FOREIGN OWNERSHIP AND THE AUTO PARTS INDUSTRY

Prepared as part of a study on

FOREIGN OWNERSHIP:

CORPORATE BEHAVIOUR AND PUBLIC ATTITUDES

for the

SELECT COMMITTEE ON ECONOMIC AND CULTURAL NATIONALISM

of the

LEGISLATIVE ASSEMBLY

PROVINCE OF ONTARIO

by

KATES, PEAT, MARWICK & CO.

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OF THE LEGISLATIVE ASSEMBLY OF ONTARIO

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The views expressed in this report are those of the Kates, Peat, Marwick & Company Study Team, and are not necessarily those of the Select Committee.

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October 18, 1973

Mr. Russell D. Rowe, MPP
Chairman
Select Committee on Economic
and Cultural Nationalism
Room 104
Parliament Building
Queen's Park
Toronto, Ontario

Dear Mr. Rowe:

This report, Foreign Ownership and the Auto Parts Industry, is submitted to you as part of the overall study of Foreign Ownership: Corporate Behaviour and Public Attitudes which we are conducting on behalf of the Committee. Auto Parts is the fourth of the six industries included in the study to be reported on in a separate volume.

We appreciate the review of earlier drafts by the members and staff of the Select Committee, and consider this input as most useful to the development of the study. At the same time we wish to acknowledge the full cooperation of those firms researched in some depth, as well as the assistance from other individuals and firms who participated in the study.

In accordance with our terms of reference this report provides factual and attitude information on the Auto Parts industry and its people, relative to the various issues of foreign ownership and control. Policy recommendations are not made since the Committee will be drawing its own conclusions based on this and other information before it.

We have attempted to make the report as complete and objective as possible within the context of available time and resources, and we trust that it will assist the Committee in its deliberations.

Yours truly

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AUTO PARTS INDUSTRY

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I - INTRODUCTION

The Ontario Select Committee on Economic and Cultural Nationalism commissioned six industry studies which were designed to examine:

- existing and potential behavioural differences, if any, between Canadian-controlled and foreign-controlled firms in these industries
- probable management attitudes to government policy initiatives with respect to the industry
- the attitude of employees of foreign- and Canadian-controlled firms regarding questions such as job satisfaction, industry issues, and nationalistic sentiments.

This sub-study report describes the approach, findings, and conclusions with regard to the Auto Parts industry.

Section I of this report briefly describes the approach adopted in this sub-study. Section II examines the industry and discusses the industry's products, markets, and other features. Section III describes the perceived and actual behavioural differences between Canadian-controlled and foreign-controlled auto parts firms. Section IV discusses executive attitudes to certain possible government policies. The conclusions drawn from this study, and a discussion of possible policy considerations are contained in Section V.

SELECTION OF THE AUTO PARTS INDUSTRY

The Auto Parts industry is one of the two manufacturing industries chosen for examination by the Select Committee. The choice of the Auto Parts industry reflects the significance of the industry in relation to a number of important factors:

- the industry in Canada is largely an Ontario industry and a major employer in the province
- the industry is an important part of the province's secondary manufacturing activity
- the industry has a favourable balance of trade with the United States
- the industry is influenced by government action, particularly with regard to the Canada-United States Auto Pact and is one of the few examples of an industry which is rationalized on a continental basis
- the industry is known to be predominantly foreign-controlled
- the industry is largely dependent for its market on the foreign-controlled automobile manufacturers operating in Canada and in the United States.

As discussed in Section II of this report, the industry is not well defined because of a multiplicity of products manufactured by firms which are not always identified as Auto Parts manufacturers. Thus, the importance of the industry and the significance of foreign control is potentially greater than a simple examination of industry statistics may suggest.

FIRMS STUDIED AND INTERVIEWED

In this examination of the Auto Parts industry seven firms were studied by direct interview with senior executives, and by the completion of a statistical questionnaire. The choice of these seven firms was designed to provide:

- size variations and different degrees of autonomy
- product differences to reveal variations in behaviour with regard to research and development, selling methods, and levels of technology
- variations in policy regarding the use of foreign nationals in senior positions
- a range of Canadian firms including a subsidiary of a group whose primary interests are not in the automotive parts industry, as well as firms specializing in this industry only.

Comparative details of the seven firms studied are shown in Exhibit 14, opposite page 27. Three of the seven firms were Canadian-controlled. One of these three was a subsidiary of a major Canadian-controlled corporation with wide ranging business interests. Three others were foreign-controlled, one of which was a small firm, and one of which was very large by Canadian standards. The seventh firm although technically foreign-controlled, is in practice subject to 50:50 control of all major policy decisions.

In this examination of the industry the seven firms were studied by direct interview with senior executives, by statistical survey

of the firms examined and by literature and other statistical research. The chief executive of each firm was interviewed, and other senior executives were also interviewed as necessary, according to the size of the firm. The interviews were structured to cover the questions set out in Appendix A. Interviews were also held with other people associated with the industry, including:

- an industry association representative
- a trade union representative
- three other executives in the industry
- two representatives of the Federal Government Department of Industry, Trade and Commerce.

Within the Federal Department of Industry Trade and Commerce there is an automotive trade policy section that carries out studies and analyses of the impacts of the auto pact. Work programs cover such areas as employment, production, investment, and rationalization in the North American automotive industry. Publications by the Department were used in this study. In addition, other published information was used, in particular:

- information published by Statistics Canada
- the sixth annual report of the President of the United States to Congress on the operation of the Automotive Products Trade Act of 1965 published in February, 1973
- studies of the Auto Pact and its effect, particularly:
    - the United States - Canadian Automobile Agreement by Henrik O. Helmers (1967)

- the Canada - U.S. Automotive Agreement: An Evaluation by Carl E. Beigie (1970).

The approach adopted in this study concentrates on the experience, opinions, and attitudes of the senior executives of the seven firms examined. Broad statistical analysis is used primarily to relate the empirical information obtained to the Auto Parts industry as a whole. In such a heterogeneous industry as the Auto Parts industry great care must be taken in generalizing based on the perceived or actual behaviour and attitudes of a small selection of firms.

EXHIBIT 1

MANUFACTURERS OF AUTOMOTIVE PARTS AND ACCESSORIES

NUMBER OF MANUFACTURING ESTABLISHMENTS AND EMPLOYEES

	ESTABLISHMENTS		EMPLOYEES (000)	
	ONTARIO	TOTAL CANADA	ONTARIO	TOTAL CANADA
1962	105	131	21.4	22.2
1963	110	136	24.6	25.4
1964	123	154	28.4	29.4
1965	127	160	30.8	32.0
1966	140	174	33.4	34.8
1967	143	178	33.5	34.9
1968	143	179	38.2	39.5
1969	139	178	40.1	41.5
1970	139	182	37.4	38.9

Source: Statistics Canada

Note: The figures shown above are not a satisfactory indicator of the establishments and employees in the Automotive Parts and Accessories industry -- see text.

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II - INDUSTRY BACKGROUND

A PROFILE OF THE CANADIAN AUTO PARTS INDUSTRY

Auto-Parts Firms

The Canadian auto parts industry is largely an Ontario Industry. In 1970 96.2 per cent of all employees in the industry, as reported by Statistics Canada, were working in Ontario. Most of the remaining employees were in the Province of Quebec. Exhibit 1 opposite shows the number of establishments in Ontario and in Canada for the years 1962-1970. In 1970 76.4 per cent of all reporting manufacturing establishments were in Ontario.

The manufacturing establishments reported by Statistics Canada are those firms whose business is primarily auto-parts manufacture. In addition to these firms, 590 other firms can be identified from Trade Directories. As an indicator of the size of the industry this larger number is misleading. It includes a number of firms who supply specific products for the automobile industry such as the Steel Company of Canada, Monsanto Chemical, and Minnesota Mining and Manufacturing, but such firms would not normally be considered as automotive parts firms. However, included in this larger number of firms but excluded from the small number of establishments reported by Statistics Canada, are some firms which are wholly dependent on the automobile industry. One example is a Canadian owned firm making plastic products with more than 50 per cent of its output going to the automobile industry, and a

EXHIBIT 2

AUTOMOTIVE PARTS AND ACCESSORIES

SHIPMENTS OF GOODS OF OWN MANUFACTURE, 1970 AND 1971

Description	1970 Value $'000	1971 Value $'000
Large establishments reporting detail		
Products:		
Drive train components	120,463	149,684
Engines, gasoline	371,667	546,965
Engine parts	66,634	69,062
Electrical equipment and electrically operated apparatus	89,608	121,511
Stampings, auto	61,215	86,676
Steering suspensions and front axles	142,589	175,597
Wheel and brake parts	154,027	188,369
Other parts	263,846	319,664
Amount received in payment for work done on materials and products owned by others	2,425	2,662
Less adjustment for value of sales taxes, excise duties and outward transportation charges which could not be deducted from individual commodity items described above	(5,070)	(5,102)
Adjusted value of shipments and work done	1,267,404	1,655,088
Small establishments not reporting detail	4,749	5,577
Adjusted value of shipment and work done - Total	1,272,154	1,660,665

N.B. Goods of own manufacture are those produced domestically (i.e. with Canadian value added content).

Source: Statistics Canada, Cat. 42-210

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second example is a foreign-controlled firm, the entire output of which is for the automobile industry, but which is classified in the electrical industry because of the nature of the company's product.

These examples indicate that the size and nature of the auto parts industry is not easily obtained from published statistical information. Furthermore, reference to trade and industrial directories gives a different but similarly incorrect picture. Of the seven firms examined in the course of this study two firms were not listed under the Heading "Auto Parts and Accessories Manufacturers" in Scotts Industrial Directory for Ontario, although in both cases more than 90 per cent of the output of the firm was for the automobile industry.

The firms listed by Statistics Canada are primarily auto parts manufacturers and manufacture the products listed in Exhibit 2. It should be noted that Exhibit 2, which is taken directly from Statistics Canada Catalogue 42-210, indicates only major groupings of products, and does not detail the many products which one would expect to find in such a table e.g. trim items, steering wheels, shock absorbers, etc.

In spite of the great variation in the firms, manufacturing processes and products in the auto parts industry it is possible to distinguish four broad product groupings. The first of these may be considered predominantly metal based products, requiring a high degree of technology in manufacture and with a high unit value. In this group are wheels, springs, shock absorbers, axles and frames. Generally speaking, in this group will be found the larger automotive

parts firms such as Kelsey-Hayes, General Spring Products Limited, Eaton Yale Limited, Hayes-Dana, Gabriel of Canada Limited, Canadian Acme Screw and Gear Limited, A.P Products of Canada Limited, and Budd Automotive Company of Canada Limited.

The second group of products may be considered to require less technology, are manufactured from metal and non metal products, and generally have a lower unit value. In this group are such products as metal stampings, plastic parts of various kinds, trim items, gaskets and filters, pedals and linkages, hoses, etc. The firms manufacturing these products are generally smaller than those in group one and larger in number.

The third group of products covers the wide range of "soft" products used in the manufacture of the automobile and in its servicing during use. Products in this group include paints, antifreeze and similar chemicals, solder, metal cleaners, plating chemicals, and polishing products. The firms manufacturing these products vary widely in size. The fourth group of products which can be identified covers the supply of services and equipment to the automobile parts and accessories industry and to the automotive manufacturing industry. Services in this group include plating, welding, mould manufacture, dies, tools, jigs, and fixture manufacture. These products and services are sometimes overlooked in a review of the auto parts industry in Ontario. In the 1972 directory of Canadian Automotive Parts Manufacturers 104 companies are listed under the heading "dies, tools, jigs and fixtures". On average

EXHIBIT 3

ESTIMATED* DISTRIBUTION OF CANADIAN AUTO PARTS FIRMS BY NUMBER OF EMPLOYEES

NUMBER OF EMPLOYEES	NUMBER OF FIRMS
Under 51	221
51- 100	171
101- 200	140
201- 500	128
501-1000	37
Over 1001	35
Other (not rated)	39
Total	771

* Based on data given in the directory of Canadian Auto Parts Manufacturers.

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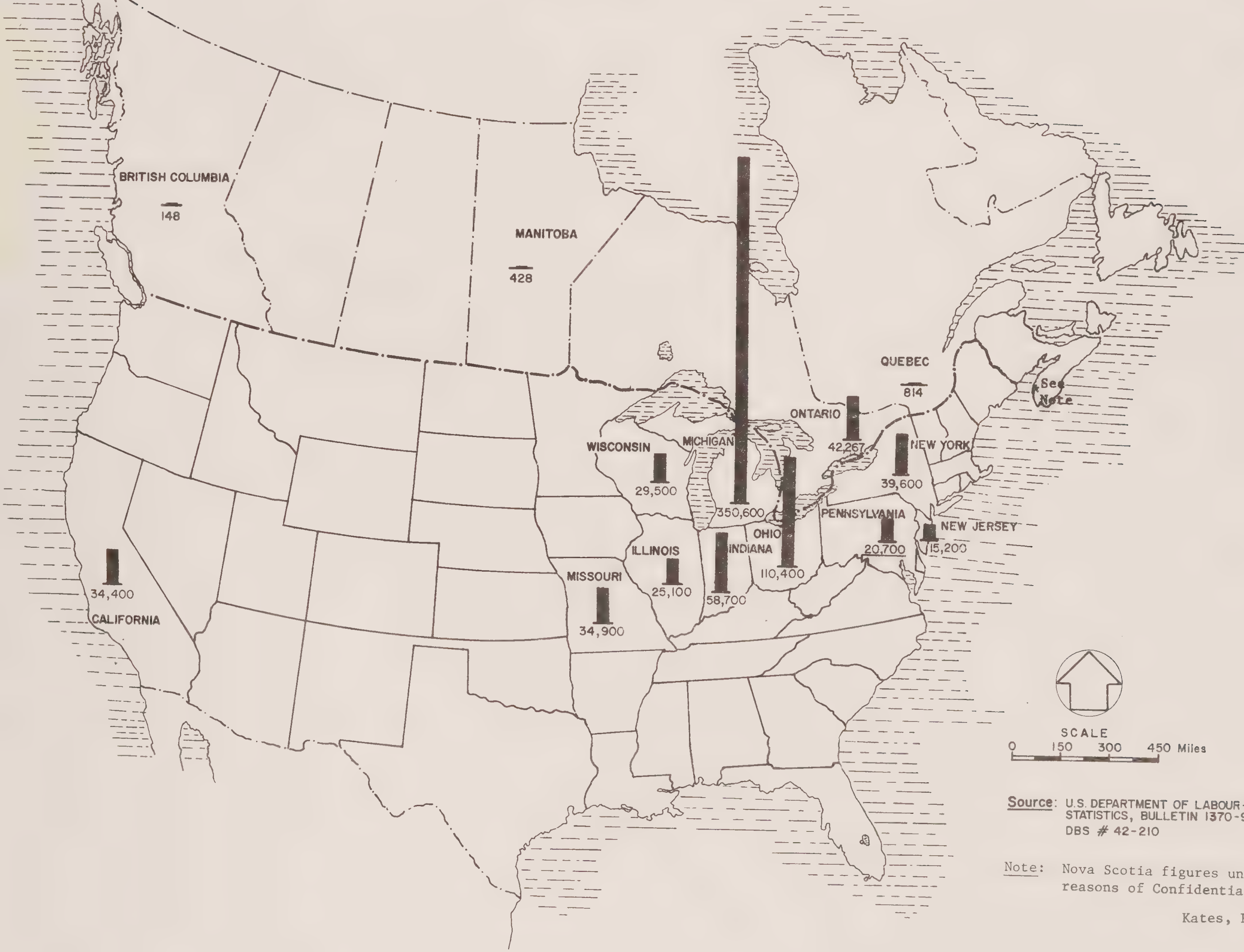
EXHIBIT 4

EMPLOYMENT IN MOTOR VEHICLES & EQUIPMENT INDUSTRY IN CANADA & U.S.

1971



Source: U.S. DEPARTMENT OF LABOUR - BUREAU OF LABOUR STATISTICS, BULLETIN 1370-9
DBS # 42-210

Note: Nova Scotia figures unavailable for reasons of Confidentiality

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these firms will be very small but employ highly skilled people.

Based on information contained in the 1972 directory of Canadian Automotive Parts Manufacturers, 392 firms, or 58 per cent of all firms recorded, have 100 employees or fewer. Exhibit 3, opposite shows the extent to which the industry is characterized by small firms.

The combined geographical distribution of auto parts manufacturing and automobile manufacture is shown in Exhibit 4, opposite. The separation of employment by province and state between vehicles and parts is not available, and in the case of United States data, in those States where employment in the vehicles and parts industry is smaller than the data shown in Exhibit 4, data is only available for the transportation industry in total (including railways, etc.). Thus Exhibit 4, should show some automotive industry employment in States such as Louisianna, New Mexico, etc. For Canada the employment in provinces other than Ontario is not shown to scale.

The concentration of employment in the north-central United States, and in Ontario, is very pronounced. This distribution has not changed to any significant extent in the period 1968-71. The improvement in economic activity in 1972 may be expected to show an increase on all 1971 employment figures, but in all the States shown in Exhibit 4 except Missouri and Ohio, 1971 employment was less than 1968 levels.

Markets

In contrast to the heterogeneous nature of the firms and products of the industry the market for auto parts and accessories has two main distinctions:

- The predominance of a small number of customers for original equipment
- the division between the original equipment market (OEM) and the after market (AM).

In North America the original equipment market is dominated by the "big four":

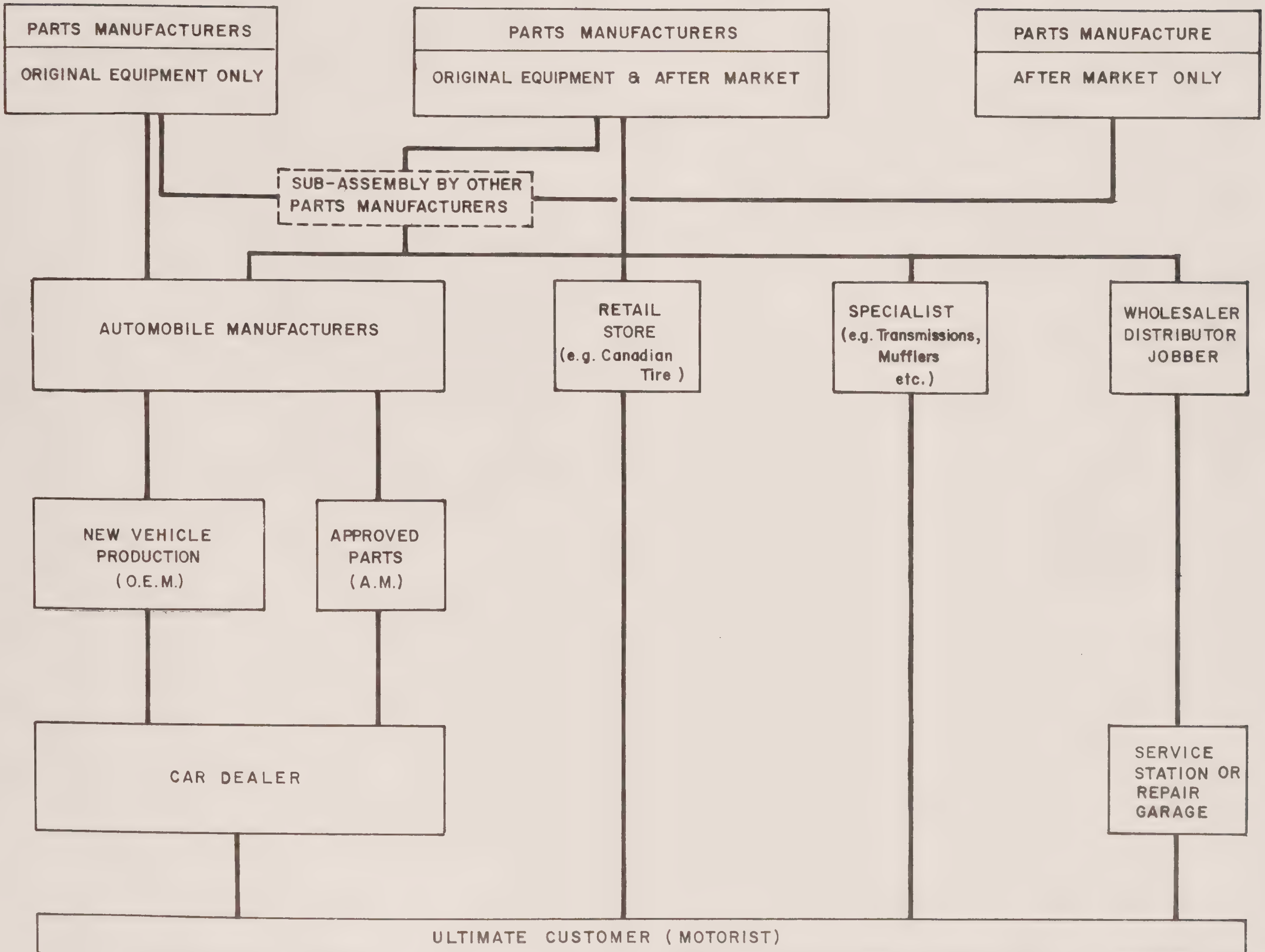
- American Motors
- Chrysler
- Ford
- General Motors

These four companies, together with International Harvester, Mack Trucks, Volvo Canada, and White Motor Corporation, make up the Vehicle Manufacturers Association.

The market system for automotive parts is shown diagramatically in Exhibit 5, opposite. For both the original equipment market and the after market, auto parts manufacturers produce parts which are sold either directly to the vehicle manufacturer or the parts distributor, or to other parts manufacturers for further work or sub-assembly prior to sale as a completed part. Of 771 auto parts manufacturers identified, 427 manufacturers supply both the original equipment and after markets. 205 companies produce only for the original equipment market, and 139 companies produce only for the after market.

EXHIBIT 5

THE MARKET SYSTEM FOR AUTOMOTIVE PARTS



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The "Big Four" automobile manufacturers dominate the original equipment market. Many automotive parts are researched, designed, and developed by the automobile manufacturer. Drawings and complete specifications are then prepared and issued to recognized suppliers of that type of part. With many parts the automotive manufacturer will also specify precisely the materials to be used, and in some cases will specify the supplier from whom the material should be purchased. The automotive manufacturer will also want to be satisfied regarding the auto parts manufacturer's ability to achieve specified quality limits, fulfill total production volumes allocated, and deliver in accordance with predetermined schedules. With these arrangements the auto parts manufacturer acts as a "jobbing shop", manufacturing to order.

For many other parts, particularly those involving more advanced and complex technology, the auto parts manufacturer is on a more nearly equal footing with the automotive manufacturer, often achieving, through specialization and the development of a particular expertise, a research, development, and manufacturing capability against which the automotive manufacturer would not attempt to compete. Product research and development activity by the auto parts manufacturer can increase the immediate percentage of the automobile manufacturer's total business for that part which the parts manufacturer can expect to obtain. However, the competitive nature of the industry and the fear on the part of the automobile manufacturer of dependance on one supplier ensures that, unless further improvements can be engineered for the next model year, any significant market share advantage will likely be eliminated in second or subsequent years of manufacture of that part. (For a detailed discussion of research and development in the industry, see pages 47-51.)

Prior to 1965 the selling activity of Canadian manufacturers of auto parts for the original equipment market was directed towards the assembly plants of the "Big Four" in Canada. Purchasing decisions with respect to Canadian assembly were taken by staff located in Canadian plants. Following the Auto Pact three of the four major vehicle manufacturers moved their purchasing activities to the United States. Ford Motor Company centralized its purchasing activity in Dearborn in 1965, and American Motors and Chrysler centralized their purchase activity with respect to Canadian and U.S. plants in Michigan in 1968. At the present time, only General Motors continues to make purchasing decisions with regard to automotive parts for Canadian assembly at its main Canadian plant.

A number of the executives interviewed in the course of this study pointed to the speed with which the decision to move was made, particularly by Ford Motor Company, and commented favourably on a decision of General Motors to continue its purchasing activities in Canada. Although the transfer to Dearborn and Detroit can be expected to have reduced the influence of Canadian nationals over purchasing decisions, at least in the long run, the growth and achievements of the Canadian auto-parts industry in the years since the transfers took place suggests that there was no significant negative impact on the economic performance of Canadian-based firms. It seems likely, however, that these moves on the part of three of the "Big Four" may have added to the difficulty that many Canadian controlled automotive parts manufacturers experienced immediately following the Auto Pact 1965, in achieving satisfactory representation at United States locations.

In the original equipment market the selling activity centres on direct contact with purchasing and engineering staff of the automobile manufacturers. This contact is by a company sales force, and/or through manufacturers' representatives in Detroit. The objective of the selling effort is to achieve a model year contract to supply a particular part or parts under satisfactory price, quality, and delivery conditions.

Many of the parts for the replacement or after market are manufactured to the same specifications and degree of control by the automotive manufacturer as already described for original equipment. This is particularly the case with replacement parts sold through the automobile manufacturers' dealer networks as "authorized" replacement parts. To the auto parts manufacturer, part numbers will distinguish between the same product in the two different markets. The parts manufacturer will also be required in many instances to package parts for the after market - as compared with the bulk deliveries for original manufacture at the auto assembly part. Some automobile manufacturers have a single purchasing authority, covering both original equipment needs and after market purchases, and others have separate purchasing divisions for these two markets.

In the case of accessories and replacement parts distributed through wholesalers, distributors, jobbers, specialists, automotive repair maintenance shops and retail stores, the auto parts manufacturer maintains a sales force to establish normal sales contact and handle problems of quality and service. Compared with the firm contracts that are established with regard to OEM purchases by the automobile manu-

facturers, the aftermarket is less certain, and quantities and delivery dates more variable. There are more purchases or purchasing points - some jobbers are nation wide, but most are provincial in coverage - and the various factors have an adverse affect on length of production run, and inventory costs. Gross profit margins tend to be higher on automotive parts for the after market than on parts for the original equipment market in order to cover the market circumstances outlined above.

Economic Factors

The degree of price competition in automotive manufacturing emphasizes the importance of lowest prices in obtaining auto parts business. Price is not the sole criterion, since mass production demands quality products manufactured to within precise limits, and for the OEM the complexity of production scheduling demands strict delivery schedules. These three factors - price, quality and delivery - determine the competition in the industry. For many products, except those protected by proprietary interest and patents, the ability of the automotive manufacturer to manufacture automotive parts "in-house" provides some permanent measure of control over automotive parts firms.

The ability of independent parts producers to compete with automotive manufacturers is due in part to the differential between the prime labour rates paid by the automotive manufacturers, and the secondary rates commonly paid by auto parts manufacturers. As Exhibit 6, overleaf, shows average hourly earnings in motor vehicle manufacture and auto parts manufacture vary significantly, with a differential of 61¢ per hour in 1972.

EXHIBIT 6

RELATIVE EARNINGS IN CANADIAN AND UNITED STATES AUTOMOTIVE INDUSTRIES, 1964-70

(Average hourly earnings)

YEAR	CANADIAN VEHICLES (1)	CANADIAN PARTS (2)	U.S. VEHICLES AND EQUIPMENT (3)	U.S. VEHICLES AND EQUIPMENT (4)	PERCENTAGES	
					(1) OF (4)	(2) OF (4)
	$(Can.)	$(Can.)	$(U.S.)	$(Can.)		
1964	2.68	2.47	3.21	3.47	77.2	71.2
1965	2.87	2.61	3.34	3.61	79.5	72.3
1966	2.94	2.65	3.44	3.72	79.0	71.2
1967	3.10	2.78	3.55	3.84	80.7	72.4
1968	3.49	3.03	3.89	4.21	82.9	72.0
1969	3.71	3.25	4.10	4.43	83.7	73.4
1970	4.06	3.52	4.23	4.42	91.9	79.6
1971	4.45	4.04	4.72	4.73	94.0	85.4
1972	4.96	4.35	5.11	5.08	97.6	85.6

Source: Statistics Canada (Catalogue No. 72-003) and United States Bureau of the Census, Statistical Abstract.

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Between auto parts manufacturers competing for the same labour the emphasis is on cost control, particularly on labour efficiency. This in turn requires optimum use of capital intensive production processes, and maximum use of long production runs. This does not exclude the opportunity to profit from highly flexible production lines which are suitable for quick changeover from one product to another. Such flexibility can enable a firm to compete effectively on products with a more limited volume.

In the case of many of the products manufactured in the auto parts industry it is easy to enter the business from a manufacturing or technical point of view. In other product areas entry is technically extremely difficult because of the investment required in specialized machinery, and because of the technical "know how", in some cases coupled with patent protection.

In those cases where entry into the business is technically easy i.e. the manufacture of plastic or metal stampings and similar products, access to the market for original equipment depends on the ability to satisfy the conditions laid down by the automotive manufacturers. The automotive manufacturers are influenced by the known ability of existing suppliers to meet quality and delivery standards and as a result companies seeking to achieve the "supplier lists" are subject to the closest examination, particularly with

regard to quality control methods, manufacturing methods, and ability to supply in volume according to pre-arranged schedules. Given the nature of the automobile industry, its emphasis on volume production and cost control, these strictures are understandable. However, for many companies trying to establish themselves as suppliers to the industry, the control exerted by the automobile manufacturers can determine whether or not the company stays in business.

The powerful position of the automobile manufacturers vis-a-vis the many smaller automotive parts manufacturers, emphasizes the need for competent professional selling effort on the part of Canadian companies. The greatest emphasis must rest on the efforts of auto parts manufacturers to develop the most efficient manufacturing processes and techniques in order to meet the necessary quality standards and compete effectively on price. Given the competitive nature of the automobile industry and the auto parts industry, entry into the market by new companies, and maintenance of a market position by existing companies, depends upon constant management attention to, and the necessary investment in improved managing techniques.

Growth in Trade After 1965

Under the stimulus of the Automotive Pact, trade between the United States and Canada grew substantially. Prior to the agreement, the tariff served to encourage the proliferation of model manufacture in Canada and hence run lengths were short, both for automotive manufacturers and automotive parts manufacturers. One major result of the Auto Pact

was the rationalization of models between automotive plants in the United States and in Canada. This enabled parts manufacturers to achieve larger production runs because of increased Canadian production of motor vehicles (see Exhibit 7) and as a result of new opportunities to supply U.S. plants.

The major growth in trade between the two signatories of the Auto Pact occurred in both motor vehicle production and auto parts production. Partly as a result of automotive assembly rationalization between the U.S and Canada, motor vehicle production in the period 1965-1972 increased in Canada by 174.1 per cent. In the United States, motor vehicle production in 1972 was slightly more than in 1965. This is shown in Exhibit 7 overleaf. The resulting increase in two-way trade in both motor vehicles and automotive parts is shown in Exhibit 8 overleaf.

There is some difference between Statistics Canada figures and United States figures regarding the actual size of the favourable Canadian trade balance on automobiles and parts. Based on Statistics Canada figures Exhibit 8 shows the extent to which very large increases in both exports and imports of vehicles and parts occurred in the years following the Auto Pact. Canadian Exports of vehicles increased in value from $66 million to $2,062 million in the period 1965-1971. In the same period vehicle imports rose from $125 million to $963 million. Canadian exports to the United States of motor vehicle parts and accessories rose from $141 million to $1,341 million, and imports from $798 million to $2,248 million. This gives a favourable Canadian trade balance of $192 million in 1971. U.S. Department of Commerce figures indicate a positive trade balance of $197 million in 1971 for Canada.

EXHIBIT 7

AUTO ASSEMBLY RATIONALIZATION

MOTOR VEHICLE PRODUCTION

1965-72

000 UNITS

YEAR	PASSENGER CARS		TRUCKS AND BUSES		TOTAL	
	U.S.	CANADA	U.S.	CANADA	U.S.	CANADA
1965	9,335	707	1,803	140	11,138	847
1966	8,605	685	1,792	188	10,396	872
1967	7,413	708	1,611	212	9,024	920
1968	8,849	889	1,972	261	10,821	1,150
1969	8,224	1,036	1,982	317	10,206	1,353
1970	6,550	941	1,734	253	8,284	1,194
1971	8,580	1,083	2,084	263	10,664	1,347
1972 (1)	8,828	1,155	2,475	320	11,303	1,475
1972 as % of 1965	94.6	163.4	137.3	228.6	101.5	174.1

Source: U.S.: Automotive Manufacturers Association

Canada: Statistics Canada

(1) Preliminary

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EXHIBIT 8

INCREASE IN TWO-WAY TRADE

A. NEW PASSENGER AUTOMOBILES

Year	Canadian Exports to U.S. (000 Units)	Canadian Exports to U.S. ($ Millions)	Canadian Imports from U.S. (000 Units)	Canadian Imports from U.S. ($ Millions)
1965	31.7	66	46.4	125
1966	146.8	346	114.7	315
1967	311.0	816	238.6	663
1968	472.5	1,257	308.4	897
1969	676.1	1,716	291.4	879
1970	696.7	1,647	252.4	660
1971	794.9	2,062	355.1	963

B. ALL MOTOR VEHICLE PARTS

Year	Canadian Exports to U.S. ($ Millions)	Canadian Imports from U.S. ($ Millions)
1965	141	798
1966	348	1,025
1967	471	1,204
1968	741	1,653
1969	1,071	2,136
1970	1,024	2,113
1971	1,341	2,248

SOURCE: Statistics Canada

Since the Auto Pact in 1965, the greatest degree of change has occurred in the export of Canadian made vehicles to the United States. Exports increased 3124 per cent. In 1965 trade between the two countries in parts and accessories showed an excess of Canadian imports over exports in a ratio of 5.6 to 1. Between 1965 and 1971 Canadian parts and accessories exports rose 951 per cent while imports rose 282 per cent. The ratio of parts imports to exports in 1971 was 1.7 to 1.

Statistics Canada figures do not separate original equipment trade from after-market products. United States figures distinguished between these markets in the case of Canadian exports only. Based on United States figures, Canadian exports of original equipment parts to the United States increased from $116 million in 1965 to $1,540 million in 1971.

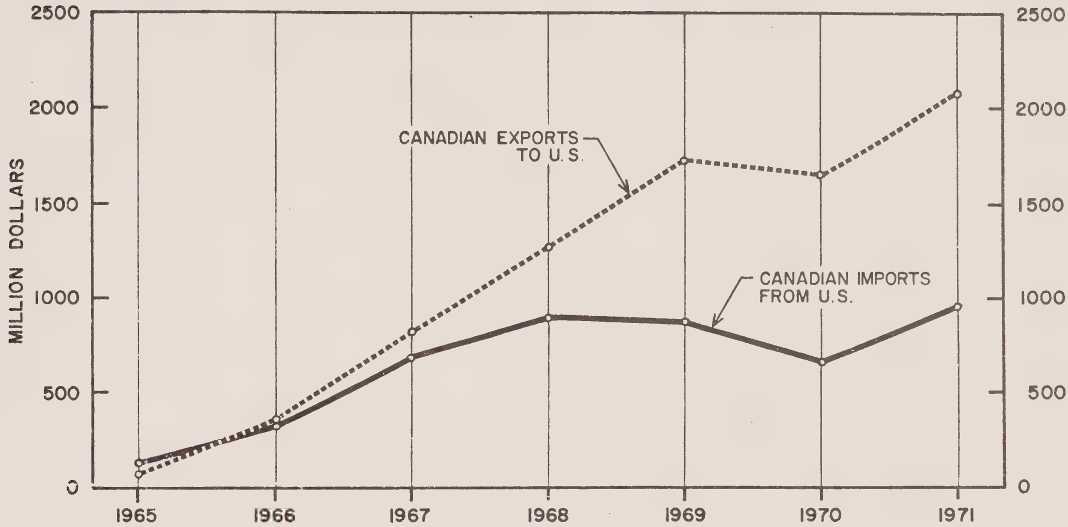
In contrast, exports of parts for the after-market increased from $52 million in 1965 to only $152 million in 1971. The after-market was not covered by the 1965 Auto Pact.

The growth in automotive vehicle and parts trade between Canada and the United States is shown graphically in Exhibit 9 opposite.

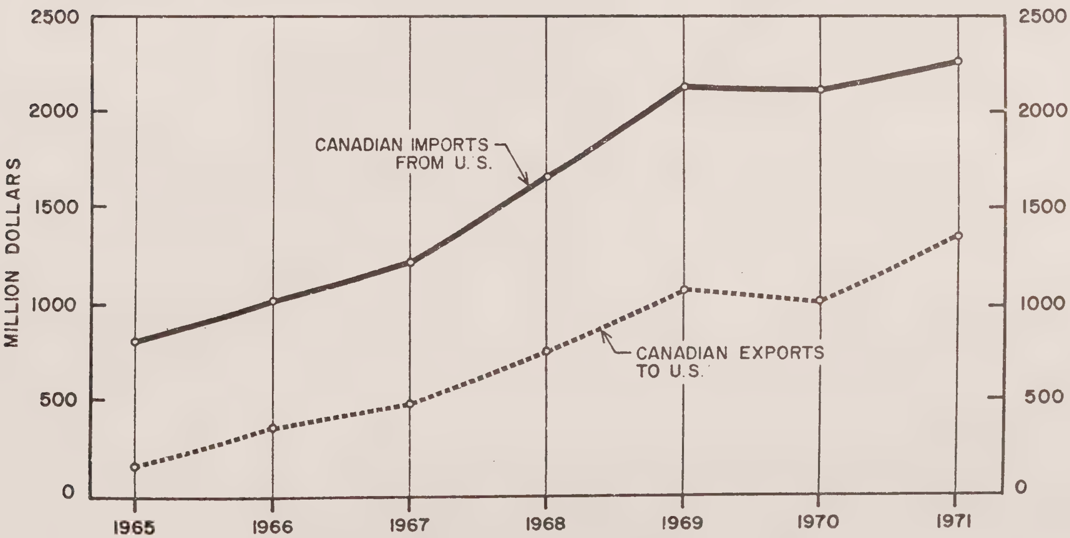
EXHIBIT 9

TRADE IN AUTOMOTIVE PRODUCTS, U. S. AND CANADA 1965 – 1971

MOTOR VEHICLES



MOTOR VEHICLE PARTS



SOURCE: STATISTICS CANADA

Kates, Peat, Marwick & Co.

EFFECT OF THE AUTO PACT ON THE AUTO PARTS INDUSTRY IN CANADA

The agreement between the United States and Canada concerning trade in Automotive products between the two countries was signed in January 1965. The objectives of the agreement were to create a broader market for automotive products, to achieve the full benefits of large scale production and specialization, and to liberalize trade from previous tariff barriers.

The Auto Pact had far reaching consequences for the auto parts industry in Canada. The advent of the Pact was viewed with alarm by many manufacturers, and as an unprecedented opportunity by many others. In essence, the Auto Pact provided two factors which, until 1965, had been lacking in the auto parts industry in Canada:

- longer production runs (for Canadian and U.S. markets) which placed a premium on efficient processes, minimum breakeven points, and an increase in capital investment in production equipment
- the exposure of the industry to competition from United States auto parts manufacturers.

The guarantees regarding Canadian content in vehicles of Canadian manufacture might have limited the extent of this increase in competition from U.S. manufacturers. However, the eagerness of non-Canadian companies (largely from the U.S.) to expand, set up, or acquire manufacturing facilities in Canada resulted in a high degree of competition for the expanding auto parts market. Among the advantages to Canadian-based companies exporting auto parts to the United States were

the favorable Canadian dollar discount, and the differential between United States and Canadian wage rates. Both factors were particularly significant in the early years of the agreement but have since diminished.

As part of the agreement, certain conditions were included with regard to Canadian content in Canadian built vehicles, and the continued growth of Canadian vehicle manufacture. Under the agreement Canadian content in Canadian produced vehicles must not fall below the dollar value achieved in the 1964 model year. Canadian vehicle production in terms of net sales value must be the higher of 75 per cent, or the 1964 model year percentage, of a manufacturer's sales in Canada.

Letters of Undertaking were furnished by the big four producers to the Canadian Government whereby the producers agreed that by the end of the 1968 model year they would increase their value added in Canada by an amount equal to 60% of the growth in net sales value of cars and 50% of the growth in net sales value of commercial vehicles sold in Canada, plus a total of $260 million divided as follows:

	Increase in Value Added in Canada Between the 1964 and 1968 Model Years	
	$ Million Cdn.	$ Million U.S.
G.M.	121.0	111.9
Ford	74.2	68.6
Chrysler	33.0	30.5
A. Motors	11.2	10.4
Others	20.6	19.1
	260.0	240.5

With these conditions, the agreement was less than a free trade agreement, and the guarantees contained in the agreement gave Canadian manufacturers a certain level of protection against the risks inherent in complete free trade between the two countries. Prior to the agreement the Canadian tariff on completed vehicles was 17.5 per cent. The U.S. Tariff on completed vehicles ranged between 6.5 per cent and 8.5 per cent, with 8.5 per cent on most automotive parts. The Canadian tariff on automotive parts was 17.5 per cent on certain specified parts and 25 per cent on others. Prior to 1965 these tariffs had been effective in inducing automotive manufacturers to assemble vehicles in Canada, and encouraged the development of the domestic parts industry to supply Canadian vehicle assembly.

At the individual company level it is difficult to generalize on the effect of the Pact. Many companies were unable to adjust to the new conditions. Prior to the agreement , limited competition resulted in high gross margins, and many entrepreneurs could not reconcile the decline in margins with the heavy capital investment necessary to maintain competitive prices. Others saw the opportunity of longer runs and greater volumes, and the ability this provided to compete favourably within Canada and in the United States, based on good management principles, cost control, and labour efficiency. Faced with these opportunities the majority of Canadian based manufacturers, both foreign-controlled and Canadian-controlled, continued to prosper. Some Canadian companies, aware of the increased competition resulting from the Pact, sought links (through ownership or otherwise) with U.S. firms in order to have access to advanced technology or to the financial resources necessary for investment in new equipment.

A typical case is company 'X' which, prior to the Auto Pact, was aggressively and successfully competing in the supply of high value precision parts. After the Auto Pact the company entered into partnership with a United States company, the latter company seeking an investment in a Canadian company in order to obtain Canadian "value added" in accordance with the Pact's requirements. Under the terms of this partnership the Canadian company obtained, primarily, technical expertise and skilled personnel. Financial support for expansion purposes was also a factor. In return the U.S. company acquired part ownership of the Canadian company, although this does not extend to full control. The source for the initiative for this arrangement is unclear. The partnership has been very successful, since the technical assistance obtained from the U.S. partner has enabled the company to achieve considerable growth and a very strong market position. The company expanded its Ontario operations and created 200 additional jobs in the late 1960's and Canadians fill all the key management positions.

It is suggested by some executives in the industry that, in the immediate years after the 1965 Auto Pact some Canadian-owned firms went out of business, or sold to other firms (both foreign and Canadian-controlled). However, the significantly adverse level of productivity in the Canadian auto parts industry prior to the pact was in many individual instances sufficiently corrected in the years immediately following the pact to enable Canadian owned and based firms to survive independently and compete successfully in many product areas.

Productivity

This improvement in production efficiency was probably continuous after 1965, and was given some urgency by the objective of the United Automobile Workers' Union of bringing Ontario labour rates up to the level of secondary labour rates in the auto parts industry in the Northern United States. It is estimated* that, prior to the Auto Pact, Canadian auto parts employees were paid about 30 per cent less on average than their U.S. counterparts. At the present time many Canadian firms, particularly those in Southern Ontario, pay labour rates close or equal to those in the industrial United States.

Statistics of industrial productivity in Canada in the period 1961-1969 show that the Motor Vehicles and Parts Industry (vehicles and parts are not separated) achieved the highest increase in productivity of any industry - an increase during the period of 199 per cent. With the closing of the productivity gap - and many executives in the Canadian auto parts industry claim that both methods and labour efficiency in the best Canadian companies are comparable with those of the best United States companies - the competitive situation of the industry has shifted to such areas as freight costs, delivery, and quality.

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* See discussion of productivity in "The Canada-U.S. Automotive Agreement: An Evaluation" by Carl E. Beigie, published by the Canadian-American Committee, 1970.

Some executives pointed to the adverse effect of social problems e.g. drug abuse, on productivity in some United States plants, and emphasized the importance, economically as well as socially, of avoiding the same development in Canada.

Capital Expenditure

The Auto Pact created an immediate need for capital expenditure to finance the expansion of production facilities and to replace inefficient equipment. Figures of capital expansion in the industry show no consistent pattern, but the surge of investment, particularly in machinery and equipment, is clear as shown in Exhibit 10 overleaf.

The need to finance major additions to plant and equipment was a considerable burden to auto parts manufacturers, particularly smaller firms or those without recourse to large 'parent' corporations. To assist firms to adjust to the new market environment created by the Auto Pact the Automotive Adjustment Assistance program (AAA) was introduced by the Federal Government in 1965. Loans at current rates of interest are made available to manufacturers in Canada of original equipment parts providing, inter alia, that financing through normal channels is not available. The program does not distinguish between foreign- and Canadian-controlled companies.

Between 1965 and 1973 loans authorized under the program totalled $114.1 million spread over 120 separate loan agreements.

EXHIBIT 10

CAPITAL EXPENDITURES BY CANADIAN AUTOMOTIVE INDUSTRIES (1960-1971
(Millions of Dollars)

Year	VEHICLES		PARTS		Total[1]
	New Non-Residential Construction	New Machinery And Equipment	New Non-Residential Construction	New Machinery And Equipment	
1960	10.3	13.0	1.5	4.8	29.6
1961	8.7	12.9	.7	6.4	28.7
1962	5.4	7.7	2.3	18.0	33.4
1963	16.6	18.5	3.0	19.7	57.8
1964	22.5	26.4	13.9	45.6	108.3
1965	39.8	50.5	17.7	88.9	196.9
1966	29.2	27.9	48.1	101.6	206.8
1967	37.2	41.3	10.3	61.8	150.7
1968	19.2	32.3	7.9	34.0	93.4
1969	15.7	24.9	11.9	79.6	132.1
1970	n.a.	n.a.	16.9	152.7	214.2
1971	8.1	20.7	8.2	62.9	99.9

NOTE: 1. Includes truck bodies and trailer manufacturers.

SOURCE: Statistics Canada

Kates, Peat, Marwick & Co.

Changes in Ownership Structure

There is a common belief that the Auto Pact resulted in a shift of control of auto parts firms in Canada, by forcing takeovers of Canadian owned firms. There is no firm evidence that this happened to any marked degree. Some executives interviewed consider that the ownership structure - of predominantly foreign-control over auto parts firms - was in existence before the Auto Pact in 1965, and has not changed significantly since 1965.

This view is supported by Statistics Canada data on Canada's International Investment position in the period 1954-1967 (see Exhibit 12, overleaf) and by available information on takeovers in the period 1965 to 1971 (see Exhibit 11, overleaf). An examination of the Merger Register, maintained by the Mergers and Monopolies Branch, Department of Consumer and Corporate Affairs shows that mergers in the industrial category "Transportation Equipment", which includes aviation, aerospace, railways etc. as well as automotive manufacturers and auto parts manufacturers, increased in 1966 and 1967, and further increased in 1968 and 1969. However, the extent to which this increase in merger and acquisition activity represented such activity in the auto parts industry is uncertain. An examination of recorded mergers in this period indicates that in the auto parts industry up to 13 companies changed ownership in one year (1969). In 1965, of the six ownership changes which occurred in the transportation and equipment industries, five represent changes relating to firms in the auto parts industry, but in three of these cases the

EXHIBIT 11

ACQUISITIONS AND MERGERS IN THE TRANSPORTATION EQUIPMENT INDUSTRY 1962-1971

YEAR	NUMBER OF COMPANIES ACQUIRED BY A FOREIGN CONTROLLED COMPANY		NUMBER OF COMPANIES ACQUIRED BY A CANADIAN CONTROLLED COMPANY		TOTAL	
	Transportation Industry Classification	Automotive Industry	Transportation Industry Classification	Automotive Industry	Transportation Industry Classification	Automotive Industry
1971	3	1	3	1	6	2
1970	6	4	4	1	10	5
1969	13	5	14	8	27	13
1968	8	2	5	1	13	3
1967	6	2	2	0	8	2
1966	8	2	1	0	9	2
1965	3	2	3	3	6	5
1964	2	n.a.	3	n.a.	5	n.a.
1963	0	n.a.	1	n.a.	1	n.a.
1962	4	n.a.	2	n.a.	6	n.a.

Source: Merger Register, Department of Consumer and Corporate Affairs

Kates, Peat, Marwick & Co.

merger did not involve transfer of control from a Canadian to a foreign company. This pattern is repeated in subsequent years, and in 1969 when there were 27 acquisitions or mergers within this group of industries, only five appeared to involve a switch to foreign control of a firm in the auto parts industry. The recorded mergers in the auto parts industry show no discernible pattern, except for an above average number of mergers in leisure products e.g. mobile homes, and in snowmobiles. In the case of leisure products a Canadian-controlled "conglomerate" was particularly active. No major companies (with 500 employees or more) are recorded as switching from Canadian to foreign control.

It must be pointed out, however, that while no firm evidence is available to support the view that there was a significant increase in foreign control in the auto parts industry there is still room for doubt. The difficulties of statistical definition in this industry, referred to at the beginning of this report, invalidate or limit the available data on ownership and control since many firms where control may have changed would not be identified as auto parts firms.

Exhibit 12, overleaf, shows that, on the basis of total dollar investment in the automobile manufacturing firms, and in auto parts firms as recorded by Statistics Canada, the percentage of investment which is foreign-controlled did not change significantly during the period 1954-1967. The proportion of foreign-controlled investment varied between

EXHIBIT 12

AUTOMOTIVE VEHICLES AND PARTS MANUFACTURE

INVESTMENT CONTROL, 1954-1967

Year	Estimated Total Investment ($ Millions)	Foreign-Controlled Investment ($ Millions)	%
1954	292	277	94.9
1955	335	322	96.1
1956	375	356	94.9
1957	386	365	94.6
1958	382	369	96.6
1959	407	393	96.6
1960	440	427	97.0
1961	467	454	97.2
1962	495	472	95.4
1963	586	559	95.4
1964	696	668	96.0
1965	815	784	96.2
1966	953	919	96.4
1967	1,059	1,018	96.1

SOURCE: Statistics Canada #67-202, Canada's International Investment Position

Kates, Peat, Marwick & Co.

94.6 per cent and 97.0 per cent. Based on this, and other available data, and the views of executives in the industry, it seems correct to conclude that the very high percentage of foreign ownership in the auto parts industry before the Auto Pact probably did not significantly increase as a direct result of the Pact, nor did it decrease.

III - BEHAVIOURAL DIFFERENCES BETWEEN FOREIGN-CONTROLLED AND CANADIAN-CONTROLLED FIRMS

THE FIRMS EXAMINED

Discussions with the executives of the seven firms examined were conducted on the basis of confidentiality of information and opinions provided. The information shown on Exhibit 13 is deliberately set out in broad terms in order to prevent identification of the companies concerned. A brief synopsis of each of the seven firms is given in the following paragraphs in order to illustrate some of the particular circumstances of each firm, and to indicate aspects of behaviour among firms in this industry.

All of the firms have experienced continued growth since the Auto Pact in 1965. Except for firms C2 and C3 (both Canadian-controlled) all firms have expanded their present facilities and the number of jobs during the last five years. Two of the three Canadian firms have experienced greater difficulty during the 1970 slow down of the automotive industry, and have been unable to rely exclusively on retained earnings for capital expenditure purposes. In contrast, all of the foreign-controlled companies have been able to support their capital expenditure plans 100 per cent from retained earnings. The resulting reliance by Canadian companies on Canadian banks for their capital investment needs is discussed later in this report.

EXHIBIT 13

SUMMARY INFORMATION ON FIRMS INTERVIEWED

NOTE: To maintain confidentiality, this information is shown in broad terms. It is intended as a guide to indicate the range of firms who provided information for this study.

Firms	Control	Approximate Number of Employees in Auto Parts Manufacture	1972 SALES						1972 Research and Development Expenditure as a Percentage of Sales[7]	1972 Capital Expenditure on Canadian Equipment as a Percentage of Total Capital Expenditure	Main Source of Finance in 1972
			Total Auto Parts ($ Millions)	Market Type		Sales by Country					
				OEM %	AM %	Canada %	U. S. %	Other %	%	%	
A1	Foreign	1500-2000	25-50	100	0	39	61	0	0[5]	65[8]	Retained Earnings
A2	Foreign	100-250	5-10	66	34	OEM-63[4] AM-35	0	3 0	[6] 0	[11] 10	Retained Earnings
A3	Foreign	500-1000	15-20	100	0	59	41	0	7.4	47	Retained Earnings
B	Equally Foreign and Canadian	500-1000	15-20	61	39	52[2]	46[3]	22	0	45[9]	Retained Earnings
C1	Canadian	250-500	5-10	70	30	40	60	0	Not available	Not available	Retained Earnings and Canadian Banks
C2	Canadian	500-1000	10-15	100	0	17	83[1]	0	10	100	Retained Earnings Canadian Banks
C3	Canadian	100-250	5-10	100	0	58	42	0	Not separately identifiable	100[10]	Canadian Banks

NOTES: 1. Influenced by control of subsidiary company in U.S.

2. OEM and AM

3. OEM Only

4. OEM sales not distinguished between customers' Canadian plants and U.S. plants.

5. Although this company incurrs expenditure on process development and experimentation, pure research is a corporate function outside of Canada.

6. Corporate function, outside of Canada.

7. The figures under this heading are as reported by the companies. Where expenditure is indicated, it is likely to be for applied research, not pure research (see text for comments on companies D and F).

8. See text

9. See text

10. See text

11. See text

Kates, Peat, Marwick & Co.

Firm A1 is foreign-controlled, and part of a large international company with total sales in excess of $500 million. This firm is typical of the large auto parts firms in Canada manufacturing parts of high value and high technology. The company's product range is limited but it enjoys a strong market position and supplies very high percentages of automobile manufacturers' requirements for these parts. The company has grown by plant additions in Ontario, and has plans to diversify through acquisition if necessary, but not necessarily in the auto parts industry.

Firm A1 may be regarded as a branch plant operation, with research and development being a corporate activity in the United States. The Canadian company pays an assessment for research and development regardless of its use of research and development services. However, certain process developments, using computers, were developed by the Canadian firm. The degree of autonomy enjoyed by Canadian management is very high compared to other foreign-controlled firms, and compared to some Canadian-controlled firms. The Canadian firm is self-financing either from the capital market in Canada or from retained earnings. The Board of the company is composed equally of Canadian and United States nationals. The 1965 Auto Pact was the initial stimulus which led to the development of the company's operations in Ontario, and the company grew without acquisition. There was an initial need for skilled management and technologists because of the highly technical nature of the manufacturing operation, and United States nationals make up one half of the eight senior positions in the Canadian firm. The company is community minded, but its support of community activities is largely a personal interpreta-

tion by the president, of the company's appropriate role. The company buys Canadian equipment where possible, and during certain expansion phases incurred additional cost, and some delays, in order to support the efforts of Canadian manufacturers to supply equipment that was not previously available in Canada. The company has a "business-like" approach to lay-offs, and regards them as a fact of life in the auto parts industry because of the dependence of the industry on automobile sales.

Firm A2 is a subsidiary of a large United States corporation. The Canadian activity is small, primarily a manufacturing and warehousing operation, with sales handled by corporate personnel who do not report to the senior executive of the Ontario plant. The senior executive in Canada is a Canadian, and is the first Canadian to hold this position. The company has a limited range of products in the high value, low weight area, and enjoys patent protection in one of its two main lines. The company has been built on a United States invention and this patent protection gives it a very strong market position in North America and internationally. The Canadian plant is treated by the parent in the same way as other plants in North America, and corporate services including research and development are centralized in the United States. The "branch-plant" nature of this operation is illustrated by the degree of control exerted over sales, labour negotiations, and through financial controls. The ability of the company to seek export business is determined by the corporate office, but local personnel are satisfied that their opportunities to supply export markets are similar to those of other plants in the United States. The percentage

of export business, however, is three per cent of total sales (1972). In 1972 only ten per cent of the company's capital expenditure was spent on Canadian equipment, but this reflects in large part the specialized nature of the production equipment for the company's products, which is not available in Canada. This company is an extreme case of very minimum autonomy vested in local Canadian management, but it should be noted that in eight years the company has laid off no employees, in spite of recessions of varying degrees and a long strike at the major automotive manufacturers.

Firm A3 is foreign-controlled and part of a medium sized United States company. Sales of the Canadian subsidiary are between $10 and $15 million and total sales in North America are in excess of $50 million per annum. Firm A3 is large by Canadian standards with between 500 and 1,000 employees. The company was Canadian-controlled until the mid 1950's when it was purchased by a United States company which subsequently sold the firm to the present United States interest. The company manufactures a range of products used for sealing and trim purposes, and generally speaking the products are of low unit value. Although the manufacturing process is quite technical, the Canadian firm faces strong competition in its market from some major international, United States based corporations. The firm concentrates its sales with two of the four major automotive manufacturers, mainly because of previous difficulty in supplying the other two of the "Big Four". These difficulties centered on the amount of non-chargeable work expected of the firm by these automotive manufacturers, and the encouragement given the firm by one of the "Big Four"

to expand its facilities on the basis of existing contracts with the company, which were then divided among a larger number of auto parts suppliers.

The general policy of the U.S. parent company appears to be to allow the Canadian firm considerable autonomy, and management of Firm A3 enjoy above average freedom of decision and action for a firm of its size. The firm employs no United States nationals, and has resisted efforts of the parent firm to carry out sales representation on its behalf in Detroit. Firm A3 has developed much of its own production technology and know-how, and as shown in Exhibit 13, this firm's expenditure on research and development in 1972 was 7.4 per cent of sales revenue in that year. In its research and development activities the firm has used the Federal Government's P.A.I.T. program and has also co-operated in, and made use of, corporate research and development facilities in the United States. Sales of Firm A3 have grown by 25 per cent in five years, and the firm has expanded its manufacturing capacity during that period. Capital expenditure requirements have been met by retained earnings and no money has been borrowed from the United States parent. Most of the profits of the firm are re-invested in new production facilities, but some funds are repatriated through inter-company royalty arrangements for research and development. Firm A3 pays salaries and wages and fringe benefits which are above average for the industry, and for the region in which it is located, but the firm is aggressive towards labour management and productivity, and takes a "hard line" on lay-offs. When General Motors was struck and shut down, Firm A3 shut

down four hours later. A majority of the Board of Directors of Firm A3 are Canadian citizens.

Firm B is controlled by Canadian and foreign interests through agreements which give neither group full control. The firm has been very successful in a limited range of products of high value and requiring high technology. The firm is an example of a successful response to the Auto Pact using United States technology (and initial skilled manpower) to develop a significant market position in a specialized product area. The company has achieved a sales growth of 60 per cent in the last five years, in spite of inter-company agreements which limit the Canadian company's access to the after market in the United States. During the last five years this firm's after market sales in Canada have approximately doubled. The company has expanded its production facilities and employment, but the growth in employment, although reaching as high as 40 per cent at certain times during the last five years, has averaged less than 20 per cent over the whole of this period. This reflects the emphasis placed on productivity improvements through the investment in automatic equipment and improved manufacturing processes. The company does not go out of its way to buy Canadian equipment, and the percentage of capital expenditure on Canadian equipment has fluctuated between 40 and 50 per cent in the last five years. Firm B has been more successful in Canada than in the United States, but its dependence on a limited number of customers makes it subject to fluctuations in total sales volume as contracts are re-negotiated. The company is not active in export markets outside of North America.

Firm C1 is part of a group of manufacturing companies created over a number of years through merger and acquisition. The firm has diverse manufacturing activities in a number of divisions, and more than one division manufactures auto parts. This firm supplies the original equipment market (70 per cent) and the after market (30 per cent) with a range of products of low value and relatively low technology. The firm has grown in line with the rest of the industry, but experienced considerable difficulties during the 1970 recession, primarily because of previous over-expansion and resulting cash flow problems. The company is typical of the old established Canadian companies which were forced to change their approach to the auto parts business after the Auto Pact in 1965. Inherent in the change was the investment of additional capital in new and improved facilities, and Firm C1 made very effective use of the loans available from the Automotive Adjustment Assistance Program. The company competes with subsidiaries of United States companies in Canada and with United States firms in its sales to the United States automotive plants. Firm C1 employs a Detroit Sales Office, and considers this essential though expensive. The firm considers that there has been a change in the United States attitude to the purchase of parts from Canadian companies during 1972, and largely as a result of this, acquired a United States subsidiary which manufactures a similar range of products to those manufactured in Canada. The company has not been interested in export markets outside North America. There is evidence that this company is more reluctant to lay-off long service employees than some other comparable companies interviewed.

Firm C2 is a relatively small but fast growing and aggresively managed Canadian company. Employment has grown from approximately 200 persons in 1968 to more than 500 employees in 1972. In the same period this firm's dependence on auto parts business has increased from 70 to 90 per cent. The company is active in seeking export business outside of North America particularly in Europe, but has not achieved any success to date. The company sales are 100 per cent for the original equipment market, and a high percentage (83 per cent) is sold to U.S. customers. This percentage is higher than any other company examined. In part it reflects the company's decision to acquire a subsidiary company manufacturing auto parts in the United States, and the company has a very clear orientation towards selling activity in Detroit. The company's success in Detroit owes something to the previous experience of the president of the company in the auto industry in that city. This factor corresponds with comments made by executives in other companies on the difficulties of establishing satisfactory sales representation in Detroit, particularly after the move to the United States of the purchasing department of three of the "Big Four". Company C2 is diversifying into a wider range of auto parts, and sees its future market in the United States. A concern for increased nationalism on the part of United States firms is part of the rationale of purchasing the U.S. subsidiary. The U.S. subsidiary is managed by a Canadian. The company has recently begun some serious research and development activity, has made use of the Federal Government's P.A.I.T. program, and is pleased with the assistance given under this program.

Firm C3 is a Canadian-controlled company and is a division of a large manufacturing group which in turn is part of a very large Canadian-controlled diversified group with sales exceeding $1 billion. The president of Firm C3 has less financial authority and less general autonomy than the president of the "branch-plant" Firm A1 discussed above. Company C3 is in the highly competitive "soft" product area of the auto parts industry, e.g. trim and similar plastic items. The company manufactures 100 different parts for the original equipment market only. In the market for such parts the business is primarily a "jobbing" business where the automotive manufacturers design the parts and specify materials, in some cases specifying suppliers of material. The company considers it unnecessary and unprofitable to engage in research and development relating to the product or to materials, although there is constant attention to manufacturing methods since competitive pressures lean on production costs, and profit margins are small. Firm C3 has experienced problems with the supply of materials from Canadian manufacturers because of competing demands for these materials from the construction industry. In some specific instances difficulty in obtaining materials because of limited supply in a buoyant market has jeopardized the company's chances of maintaining some contracts with automotive manufacturers. However, the company is the second major supplier for a number of parts to one of the "Big Four".

Firm C3 found it difficult to achieve satisfactory representation in Detroit and uses a U.S. national as a Sales Manager. One immediate effect of the Auto Pact on this firm relates to its lack of experienced sales staff. Fifty-eight per cent of the company's sales are to Canadian plants, but the company regards the market as North American. The company sees little opportunity for exports of low value plastic and trim items of the type it supplies. The company is small compared to some of its stronger competitors and feels that it carries a cost penalty because of its inability to achieve larger volumes. The company feels that its larger competitors have greater technical expertise, and that this factor is important to the automobile manufacturers.

Through examination of the seven firms contacted in this study, and through other research, areas of possible behavioural differences between foreign-controlled and Canadian-controlled firms in the auto parts industry were examined.

LOCAL AUTONOMY AND DECISION-MAKING

In the context of foreign ownership, autonomy can be defined as the freedom to commit resources and enter into agreements without approval from a policy or decision-making body outside Canada. Obviously this definition does not apply to Canadian-controlled subsidiaries, since the same degree of local (i.e. subsidiary) autonomy may exist for a Canadian-controlled firm, but be subject to decisions equally remote from the auto parts industry, although made in Canada.

Based on interviews with industry executives the amount of autonomy depends on:

- company size, company commercial success, and the evolution of corporate policies (e.g. the degree of centralization, versus a policy of autonomous subsidiaries)
- the managerial strength and personality of local subsidiary management.

One measure of the extent of autonomy is the expenditure level at which higher approval is necessary. One firm which was foreign-controlled had a very low local financial approval level of less than $500. Another firm, also foreign-controlled, had a much higher approval level, but in operational practice the effective autonomy was much higher for both firms, since the Presidents of the subsidiaries enjoyed the confidence of corporate executives and in practice were able to commit the firm beyond apparent levels.

There is no firm or direct evidence that lower autonomy on the part of foreign-controlled firms will result in decisions being taken which are in favour of foreign rather than Canadian interests. In this context "Canadian interests" means the pursuit of business developments and opportunities which will maximize economic benefits for Canada and Canadians e.g. the maximization of production from Canadian facilities, the creation of new jobs, and the pursuit of export markets. The firm examined which had minimum autonomy (measured in terms of local expenditure levels and authority over sales activity and in labour negotiations) had not experienced any lay-offs in more than eight years. This was in

contrast to the "most autonomous" foreign-controlled firm. The "minimum autonomy" firm does not control its own sales activity and sales policy decisions are made at corporate level in the United States. Sales growth and volume of the Canadian operation compares satisfactorily with that of other United States based plants. 66 per cent of the firm's OEM sales are in Canada and 34 per cent in the United States. The firm does not sell into the United States after-market, but this market is not covered by the Auto Pact and thus there is an effective tariff to deter AM sales. This firm does export outside North America from the Ontario plant (e.g. to South America) and local management feel that export opportunities are allocated to Canada on a "most economic source of supply" basis. Three per cent of the firm's 1972 sales went to the export market (outside North America), and although this seems very small it is the highest percentage of the seven firms examined.

It is clear, however, that major investment decisions, and decisions regarding union contracts, expansion etc. may be taken outside Canada in the case of those firms that are foreign-controlled. On any individual decision there is likely to be no difference in the result compared with the decision of a Canadian-controlled firm except where:

- the parent corporation has wide ranging interests and alternative investment possibilities may compete with investment opportunities in Canada

- parent corporations operating in other foreign countries may be subject to local inducements to encourage investment in those countries

- firms with operations in the U.S., whether Canadian-controlled or not, may be subject to parent corporation decisions which are influenced by political considerations or domestic inducements e.g. the DISC program in the United States.

All three points above could apply to auto parts firms controlled by Canadian corporations. Specific examples of decisions taken as a result of such influences are hard to find. Many executives of subsidiary firms will not be involved in corporate capital expenditure decisions, and will frequently be unaware of the basis for the rejection of expenditure requests. However, the experience of the senior executives in the foreign-controlled firms was very similar, in that they were satisfied of their ability to obtain Corporate financial and other support for their plans and proposals either for investment in new equipment, or in expansion of operations in Canada. The President of Firm 'A1' has authority to approve up to $20,000 on single items of capital expenditure. From this limit to $100,000 the approval of two non-Canadian directors is necessary, and proposals in excess of $100,000 require approval of the Canadian board, which has 50 per cent Canadian representation. Executives in the foreign-controlled firms could not give examples of significant proposals which had been turned down at corporate level other than on grounds of inadequate financial return, and they were unaware of proposals which had failed because of more attractive investment opportunities in the United States or in other countries, although such considerations would not always be known to Canadian management. Executives felt that as long as the Canadian subsidiary's performance was good,

then their real autonomy would be great, and their plans and proposals would be approved. It seems most likely, based on the amount of control which could be exerted by the foreign parent corporation in its Canadian subsidiaries, that poor financial performance would bring much closer scrutiny of expansion and investment proposals and the individual performance of senior executives. Under such circumstances foreign corporations may limit or reduce their investment in a Canadian subsidiary in favour of investments in the home country or in other foreign countries. This would be against Canadian interests. However, it seems equally likely that, with an existing operation and substantial investment in a Canadian subsidiary, the foreign corporation would inject the necessary corporate-based expertise to remedy the declining situation. This could involve the transfer into Canada of foreign nationals.

ACCESS TO MARKETS

In the early years of the Auto Pact Canadian firms were at a disadvantage in selling products to automotive plants in the United States. In many instances Canadian firms were not experienced in making representations to U.S. plants and lacked the appropriate contacts with the "Big Four" manufacturers in Detroit. The Canadian-controlled companies interviewed were generally emphatic that it was difficult for Canadian-controlled firms to open doors in Detroit in spite of a noticeably "pro-Canada" policy on the part of many U.S. executives in the early years of the Pact.

In order to overcome this disadvantage most Canadian auto parts manufacturers have set up sales offices in Detroit and other cities, and - as is common in the industry - have frequently employed American nationals in those offices in senior sales positions. Canadian firms have followed this practice in order to obtain sales executives with experience of Detroit commercial circles and contacts with the automobile manufacturers. It was implied by some executives that the employment of United States citizens would avoid any possible adverse nationalistic attitudes on the part of the automobile companies, but this reflected their apprehensions rather than measurable effects. Canadian-controlled companies have also tended to use the services of sales agents in the Detroit area.

By comparison, some Canadian subsidiaries of U.S. corporations have been able to use the facilities of their parent corporations with the resulting direct saving in sales expenditure, and with improved effectiveness. However, it should be noted that in the case of one foreign-controlled Canadian firm interviewed (firm A3) the firm had subsequently acted independently of the parent corporation, and even taken business away from it. This particular firm enjoyed a high degree of local management autonomy.

There is evidence of changing behaviour on the part of Canadian-controlled firms in order to overcome the difficulties of selling into the United States. Executives in almost all of the firms interviewed pointed to the significant increases in "buy-American" attitudes

which developed particularly in the early part of 1972. There is a general belief that these attitudes were prompted by political and economic motives, and that Canadian firms will find it harder to sell in the U.S. market. It is significant that two of the three Canadian firms examined have established subsidiary companies in the United States in recent years and regard the availability of this alternative (U.S.) source of manufacture as giving them additional leverage in selling to U.S. automotive assembly plants. One firm with such a subsidiary has had to operate the U.S. plant at premium cost over-time rates in order to supply a motor vehicle manufacturer who has rejected requests to accept identical parts at identical prices from the company's Canadian plant. Canadian-controlled firms may increasingly find it beneficial to establish United States based plants, if "buy American" sentiments among automobile manufactures continue.

In each of the firms visited one or more of the senior executives referred to this change in United States attitudes to the import of Canadian products, and all gave 1972 as the year in which this attitude developed. In none of the firms was it possible to quantify the results of this attitude change - in terms of contracts lost - but executives had no doubt that this was a very real change of attitude. Some executives linked the change to the 1972 Presidential campaign and to political pressures to generate increased employment in Michigan.

If such a change of attitude has occurred it is too early to measure effects even if these effects are measurable. In the same way

it is difficult to measure the effect of the pro-Canada sentiments in the United States, which accompanied the 1965 Auto Pact. The obvious success of Canadian auto parts firms in selling into the United States market for original equipment based upon competitiveness in terms of price, quality, and delivery suggests that sentiment and attitude changes in response to short-term political or balance-of-trade concerns may occur from time-to-time without serious effect. However, many foreign-controlled auto parts firms are clearly susceptible to corporate sourcing decisions which take account of national (i.e. United States) needs first, consistent with acceptable profits from foreign (i.e. Canadian) subsidiaries.

EMPLOYMENT OF FOREIGN NATIONALS

Except for some senior sales positions located in the United States, Canadian-controlled companies do not generally employ U.S. nationals in senior executive positions. Of the foreign-controlled companies examined, one top executive was a U.S. citizen, and in one of the other two companies the top executive was the first Canadian to occupy that position. In the first company, three other senior executives were also U.S. citizens, but in the other two foreign-controlled companies there were no U.S. nationals in any positions.

Opinions are divided on whether the appointment of foreign nationals to senior executive positions is increasing or decreasing. Supporting the view that a foreign-controlled firm will move towards the employment of more foreign nationals are such factors as:

- the advantage for parent corporations of providing training for their nationals through appointments in Canadian subsidiary companies

- the advantage to a foreign parent corporation of having senior positions filled by nationals trained and experienced in the procedures and corporate attitudes of the parent, and thus able to manage the subsidiary in accordance with these factors. Familiarity with corporate standard information needs and systems is important in this respect, and may provide a "guarantee" of easier control than might be the case with a Canadian national.

The view that the employment of foreign nationals will decrease is supported by factors such as:

- the supply of competent Canadian management talent is probably adequate to requirements in the industry, in contrast to the situation that existed in the early and mid 1960's

- the high levels of personal taxation in Canada in comparison with, say, United States, often place foreign nationals at a considerable income disadvantage, or, alternatively, require the parent corporation to incur a compensatingly high cost.

The high incidence of taxation in Canada (compared to the United States) may be of particular concern to some U.S. executives. There is uncertainty regarding the capital gains tax liability of foreign nationals resident in Canada who have investments outside of Canada. In practice this problem of unexpected tax liability could have widespread application to a degree where a definite financial disincentive existed. In conjunction with higher levels of personal income tax, property, taxes, and some basic cost of living items (e.g. housing)

a definite deterrent to United States nationals may exist. The general view in the industry, however, is that Canada can produce adequate supplies of managerial and supervisory talent. All of the foreign-controlled companies examined had a "hire Canadian" policy, but in practice implementation of such a policy is a matter of the particular requirements of a position at any given time. On balance, and based on the opinions of those interviewed, it seems likely that the trend in the employment of foreign nationals will probably decline.

There are cases of Canadian nationals who, working for foreign controlled firms, have been transferred to senior positions in the corporation outside of Canada. Of the three foreign-controlled firms examined two examples were given of such transfers. In one case the executive had returned to Canada as a result of a subsequent transfer. One case is recorded in the industry of the president of a Canadian subsidiary being appointed president of the parent corporation in the United States.

One senior executive in a Canadian-controlled firm expressed, strongly, the view that for an ambitious man the opportunities in Canada are quickly exhausted and a move to the United States is necessary. In general, executives regard the industry as North American rather than Canadian and the movement of key people between the two countries is regarded as normal and desirable by people in the industry. During this study no evidence was found of promotion opportunities for well qualified Canadians being cut-off by rigid corporate policies regarding senior positions for which only United States nationals would be considered. Strict immigration regulations could hinder this movement between the two countries, but were not identifiable as a problem at present.

RESEARCH AND DEVELOPMENT

Many firms in the auto parts industry do little if any research and development. For many product lines research and development is very expensive, and carries a high risk. The following factors are relevant:

- the "Big Four" do much of their own research and development (virtually all of it in the United States), and use part suppliers as jobbing shops, - manufacturing parts to specifications engineered entirely by the automotive companies

- in many instances research and development of manufacturing processes is left to the manufacturers of machine tools, presses, production equipment etc. whose resources are adequate and whose expertise is appropriate for the development of highly technical manufacturing processes

- research and development in certain areas where the parts supplier has a particular technology or expertise can be important in securing premium prices and an above-average proportion of the automotive manufacturers' total purchase requirements. In these product areas, development of products is carried out in very close co-operation with engineering and design staff of the automotive manufacturers , and the auto parts supplier acts as a specialist research arm of the automobile manufacturer

- some auto parts manufacturers do "pure" research and development work, on the development of new products and/or on the development of improved production methods.

Except where a newly developed product is patentable, a company developing a new product may be able to obtain a price or market share advantage from the automotive manufacturer during the first year, before competitors are able to tool-up to manufacture

the same product. However, in subsequent years it is in the interests of the automobile manufacturers to reduce their dependence for the product on the firm responsible for its development, and so they will seek to obtain other sources of supply and reduce the market share of the developing firm.

The foreign-controlled firms interviewed were able to take advantage of corporate research and development facilities both in terms of new products and in terms of improvements to manufacturing processes. The use of an extensive corporate research capability based in the U.S. is common among the foreign-controlled firms examined. Since these firms do little if any research in Canada (see Exhibit 13, opposite page 42) the Canadian industry is largely denied the opportunity to develop its own research capability.

Firm A1 has access to very extensive corporate research and development programs in the United States, and is assessed a financial contribution towards this facility regardless of use. The products of firm A1 are subject to modification and some re-design when model changes occur but the development of entirely new products is uncommon. The corporate research effort puts considerable emphasis on manufacturing process improvements, developing and testing new techniques which can improve quality and/or productivity. Executives in this firm were also able to cite examples of local ideas which had been developed in association with corporate research staff. In general however, the firm considered it uneconomic to compete with, or attempt to duplicate the skills available at corporate level, since recourse to corporate facilities carries no significant incremental cost.

Firm A3 conducts its own research and development program and employs skilled personnel whose responsibilities are geared to the development of new products. This firm has access to corporate research facilities but the greater diversity of product within the subsidiaries of this corporation reduces the immediate value to Firm A3 of corporate research programs. However, the Canadian firm is able to refer to corporate staff for advice on specific problems, particularly relating to raw material processing, and the development of new adhesives, which is a key factor in many of this firm's products. This firm frequently engaged in its own research programs with PAIT assistance.

Firm A2 conducts no research of its own in Canada and is entirely dependent on its corporate group for new product development and process development.

It is difficult to quantify the value of corporate research and development to foreign-controlled firms, and hence equally difficult to measure the disadvantage suffered by Canadian-controlled competitors without similar support. There are probably no Canadian-controlled firms in the auto parts industry who can match the size and scope of the research and development resources available to subsidiaries of the larger United States corporations in auto parts manufacture, e.g. Rockwell International. Even the larger foreign subsidiaries (say with annual sales of up to $50 million) could probably not economically support a research and development activity of their own with an effect comparable to that now available at corporate level, for the charges the subsidiary now incurs.

It seems probable therefore that the smaller Canadian-controlled firms are at a significant disadvantage with respect to research support, and this may have channelled many Canadian companies into those product areas where product research on their part is not necessary, e.g. the highly competitive "jobbing" work over which the automobile manufacturer has complete control of design, material specification and process selection. This does not mean that Canadian controlled-firms are unable to conduct effective research and development programs but it emphasizes the importance to Canadian firms of adequate government programs to support their efforts. In some industries joint research is undertaken with costs shared among the firms participating. It is unlikely that such an arrangement would be effective in an industry composed of a large number of firms and heterogeneous products as exist in the auto parts industry.

All of the firms examined were positive with regard to the existing government programs (P.A.I.T. and I.R.D.I.A.) designed to help finance research and development activities of Canadian companies. However, the extent of aid under these two programs is not comparable to the corporate research programs to which foreign-controlled companies will frequently have access. The IRDIA program provides tax-free cash grants on 25 per cent of all qualifying expenditures during a preceding fiscal year; the PAIT program provides grants of 50 per cent of eligible current costs.

Of the three Canadian-controlled firms two did not make any significant use of the PAIT and IRDIA programs. Of the remaining four

firms, two had made use of the programs. One of these firms complained about the effort required to provide the accounting detail necessary for a PAIT grant.

There is insufficient statistical data available to indicate the distribution of research and development activity in the auto parts industry between Canada and the United States. Based on the firms examined in this study it seems likely that there is proportionately less research and development in Canada than in the United States, in relation to production. Corporate research facilities located in the United States-controlled companies. However, the technical and economic benefits which arise from these arrangements do not preclude the maintenance of an effective research and development activity by foreign-controlled firms in Canada, and a number of foreign-controlled firms maintain an active research program. It seems likely that the proportionately greater development of new products in the United States in this industry contributes to the fact that Canada is a net importer of fabricated raw materials (e.g. asbestos brake linings) in spite of our large production of the basic raw materials; the Canadian jobs and income foregone in this way would appear to be an indirect but significant disadvantage resulting from foreign ownership of the "Big Four" auto manufacturers since their "demand pull" for research and product development is felt more in the United States than in Canada.

SOURCES OF FINANCE

In order to remain competitive in the auto parts industry it

is important to invest in new equipment. Financing of capital expenditure, by both foreign-controlled and Canadian-controlled firms appears to be largely from retained earnings, together with limited use of bond issues and bank loans.

Some conclusions on sources of new finance can be drawn from the information obtained, but any detailed comparison of profitability is limited by restrictions on the information made available to the study team by the private firms, (e.g. Firms B and C2), by the divisional status of Firm C3, and by the difficulty of separately identifying the financial performance of those plants of Firm C1 which are wholly or partially engaged in auto parts manufacture. Firm A1's financial performance has fluctuated, and like many similar firms which are totally geared to the automotive industry the company experienced poor results during the 1970-71 period, which also coincided with major expansion. In 1972 the company produced excellent financial results. In 1972 Firm A1's capital expenditure was around $3 million, and this was financed entirely by retained earnings. This firm is financially independent of its parent in the United States, and there are no cash pooling arrangements.

By contrast Firm A2, the foreign-controlled subsidiary with minimum autonomy, is subject to corporate cash-pooling arrangements and strict financial controls. This firm obtains capital finance from within the corporate system, but in 1972 the firm's retained earnings financed its capital investment needs.

Firm A3, a foreign-controlled subsidiary with a high degree of local autonomy, has never found it necessary to obtain finance from the parent organization in the United States. In 1972 the $1-1/2 million capital expenditure program undertaken by this firm was entirely financed by retained earnings. If profits were insufficient to finance capital expenditure requirements, this firm would look to the chartered banks for necessary financing. In this respect the firm would act in the same way as Canadian-controlled firms in similar circumstances, although if this source failed, then Firm A3 would turn to its parent for funds. Funds in excess of investment needs are repatriated to the United States, but in the last five years a major proportion of profits has been re-invested in Canada. This firm has royalty agreements with the parent corporation through which some transfer takes place.

The Canadian-controlled companies also relied primarily on retained earnings to finance capital expenditures. Firm C1's retained earnings in the period 1967 through 1970 varied between $0.7 million and $1.4 million. This firm has also substantially increased its long-term debt during the last five years from $200,000 to $2,000,000, and the majority of the debt has been financed through the Automotive Adjustment Assistance Program. This firm has been in very tight cash circumstances at various times since the Auto Pact, mainly because of acquisitions (of auto parts firms and firms in other businesses), expansion of production facilities, and outlays for research and engineering. This firm has not paid dividends since 1968.

Firm C2 was reluctant to give financial details. In 1972 the firm's unspecified capital expenditures were financed half by retained earnings and half by Canadian banks. All of Firm B's 1972 capital expenditure of $240,000 was financed by retained earnings. Neither firm had experienced exceptional or unusual difficulties in raising money from banks.

Firm C3 is a subsidiary of a Canadian-controlled group, and cash pooling arrangements operate. Retained earnings and bonds are the main source of finance. This firm is in a very competitive sector of the market (with main competition coming from United States firms) and, in the opinion of one executive, would have ceased operations, or sought a merger, at the time of the 1970 recession, had it not been able to obtain support from the parent group.

Executives in both foreign-controlled firms and Canadian-controlled firms refer to the lack of risk capital in Canada and the allegedly conservative attitude of the chartered banks. One company described a situation in which a major export contract for certain of its non-automotive products required a substantial investment in expanded production facilities. The credit risk of the business was already underwritten by a government agency. The firm's regular Canadian bank required two weeks to give a negative reply to the firm's request for funds. A non-Canadian bank approved the request, on the basis of the same information, after two days of examination. There was a general feeling among executives in Canadian-controlled firms that government

aid along the pattern of the automobile adjustment assistance program should continue to be available - to all firms in the industry, foreign- and Canadian-controlled.

CONDITIONS OF EMPLOYMENT AND EMPLOYEE RELATIONS

The concentration of auto part firms in Southern Ontario, and the need to compete for labour means that any individual firm is unable to vary far from the norm with regard to conditions of employment, fringe benefits and wage rates. In the same way, trade union activity tends to result in an equalization of wage rates in a given location, regardless of controlling ownership. Under these circumstances, only above average achievements in productivity and labour management can support the payment of premium rates or above average fringe benefits. In general therefore wage rates for similar classes of labour vary relatively little between firms, except on a geographical basis - labour rates in Parry Sound may be 50¢ to $1.00 per hour below those paid in Windsor.

There appear to be no differences in behaviour between foreign-controlled and Canadian-controlled firms with regard to hiring employees, and lay offs. In an industry in which one customer may account for over 60 per cent of a particular product line - perhaps accounting for more than 50 per cent of the company's total auto parts business - the ability of the customer to close down the auto parts plant as a result of industrial disputes, or for production and quality reasons, means that lay offs are a fact of life. No auto parts firm can afford to

keep on labour unnecessarily and no behaviour differences are discernable in this regard.

A senior Canadian trade union official interviewed during the course of the study was of the opinion that as far as labour relations were concerned there were no major differences in the behaviour of foreign-controlled firms and Candian-controlled firms. In some cases subsidiaries of foreign-controlled firms made use of senior labour relations personnel at corporate level in contract negotiations with the union, and in the view of the trade union official this input was often more experienced, and resulted in smoother, more effective bargaining. The practice of using experienced corporate labour relations staff applies to Firms A2 and A3.

COMMUNITY RELATIONS

Interviews with the seven firms revealed no evidence of behavioural differences attributable to ownership with regard to community involvement. Almost all of the companies interviewed have a policy regarding the support of local charities and community affairs, and generally allocate the total budgeted amounts to "causes" in areas where their employees reside. Although specific policies with regard to community involvement and charitable support are common, the main determinant of the degree and nature of community involvement and support is the personality and interest of the president of the company. The extent and nature of this interest does not reflect the control pattern of the company.

Among the companies examined there were examples of senior executives of foreign-controlled firms who had participated to a significant degree in local community promotional activities. In general, however, for both Foreign and Canadian-controlled companies, the degree of financial support was decided in relation to past budgetary allocations and present expenditure constraints.

EXPORT ACTIVITY

Except for the market in the United States, certain factors reduce the opportunity to export auto parts to foreign markets:

- the low margin on sales, and the importance of freight costs
- the relatively high labour costs in North America compared to some other potential export markets
- the importance, in the case of many products, of close supplier and automotive manufacturer co-operation in engineering and development.

In addition, the availability of a strong growth market in the United States and in the domestic market since 1965 has almost certainly reduced the incentive for Canadian firms to seek markets outside of the North American continent.

However, opportunities in export markets still exist, particularly:

- when foreign automotive manufacturers require special shipments in order to meet supply failures on the part of usual sources

- when product exclusiveness offers a distinct competitive advantage

- when freight costs are low in relation to value

- as and when changes in relative labour costs between North America and other countries improve Canada's competitive position.

As shown in Exhibit 14, opposite, exports of auto parts to countries other than the United States have grown since 1965, but continue to be insignificant compared to exports to the United States. After the United States, Mexico and Australia are Canada's largest auto parts cuttomers.

Of the firms examined in this study none had a significant export market outside the United States. The foreign-controlled firm which did have some export business outside of North America enjoys some product exclusivity by virtue of patent rights, as well as a favourable value to weight ratio. This company's export sales out of North America are currently made to major automotive manufacturing countries in western Europe and to relatively non-industrial countries in Latin America and elsewhere. One of the Canadian-controlled companies had attempted to develop export business with a major European automotive manufacturer but without success.

A major question in relation to the industry's export potential is the freedom of Canadian subsidiaries of foreign corporations to develop their own export markets independent of corporate marketing and sourcing decisions. Based on the experience of the firms interviewed, there is some evidence of supply decisions being taken outside of Canada which

EXHIBIT 14

CANADIAN TRADE IN AUTOMOTIVE VEHICLES AND PARTS WITH ALL COUNTRIES, WITH THE UNITED STATES AND AND WITH OTHER COUNTRIES, AS COMPARED WITH TOTAL TRADE, 1964-70

(MILLIONS OF DOLLARS)

YEAR	ALL COUNTRIES			UNITED STATES			OTHER COUNTRIES		
	TOTAL TRADE	AUTOMOTIVE TRADE		TOTAL TRADE	AUTOMOTIVE TRADE		TOTAL TRADE	AUTOMOTIVE TRADE	
		Vehicles	Parts		Vehicles	Parts		Vehicles	Parts
	CANADIAN EXPORTS								
1964	8,094.2	82.2	95.2	4,271.1	26.3	70.5	3,823.1	55.9	24.7
1965	8,525.1	183.2	172.8	4,840.5	90.6	140.7	3,684.6	92.6	32.1
1966	10,070.6	602.9	432.1	6,027.7	492.9	389.4	4,042.9	110.0	42.7
1967	11,120.7	1,215.2	565.4	7,088.5	1,115.0	512.5	4,032.2	100.2	52.9
1968	13,269.9	1,888.0	908.0	8,941.5	1,740.0	846.5	4,328.4	148.0	61.5
1969	14,498.2	2,513.5	1,128.0	10,273.5	2,391.8	1,043.3	4,224.7	121.7	84.7
1970	16,401.1	2,388.5	1,228.0	10,579.9	2,286.0	1,140.8	5,821.2	151.5	87.2
	CANADIAN IMPORTS								
1964	7,487.7	175.6	642.2	5,164.3	75.4	623.4	2,323.4	100.2	18.8
1965	8,633.1	295.0	818.8	6,044.8	170.4	798.0	2,588.3	124.6	20.8
1966	9,866.4	509.1	1,170.2	7,135.6	398.2	1,136.8	2,730.8	110.9	33.4
1967	11,075.2	852.2	1,405.7	8,016.3	738.2	1,370.9	3,058.9	114.0	34.8
1968	12,358.0	1,208.3	1,948.6	9,048.4	1,022.0	1,900.6	3,309.6	186.3	47.8
1969	14,130.4	1,340.7	2,494.1	10,243.2	1,085.7	2,425.0	3,887.1	255.0	69.1
1970	13,951.9	1,224.2	2,312.3	9,917.0	969.4	2,212.8	4,034.9	254.8	99.5

SOURCE: Statistics Canada, Estimates of Canada's Foreign Trade in Motor Vehicles and Parts, 1964-70

limit the freedom of Canadian subsidiaries to supply other export markets. Firm A2 is very much a "branch plant" operation, with corporate staff in the United States responsible for sales policies and activities. This firm manufactures and delivers as directed, and Canadian management has no influence over sourcing decisions relating to North American or export markets. However, as noted earlier in this report, this firm was exporting to South America, and exported to various countries at various times. There was no set pattern. It was not possible to establish whether the Canadian firm was obtaining a "fair share" of the corporation's total export business sourced from North America, but Canadian management were satisfied that the firm did supply export business in proportion to its size and competitiveness vis-a-vis other corporate plants in the United States. It should be noted that, although not always a factor, the recent export business to South America had been influenced by the Canadian currency to which the customer had access and this was known to be a factor in the sourcing decision. In 1972 Firm A2 sold three per cent of its production outside of North America - the highest figure among the seven companies examined.

The question arises as to whether the Canadian auto parts industry currently exports to countries outside North America to an extent comparable with the industry in the United States. The table below compares Canadian and United States exports and imports to other countries in 1971.

	Canada ($ million)	United States ($ million)
Auto parts production	1,660.7	16,012.5
Exports to other countries	78.0	722.0
Exports as per cent of production	4.7	4.5
Imports from other countries	87.0	431.0
Imports as per cent of production	5.2	2.7

In 1971 exports as a percentage of production totalled 4.7 per cent for Canada and 4.5 per cent for the United States. There was a significant difference in the relationship between imports and production with Canadian imports at 5.2 per cent of Canadian production being double the level in the United States, mainly as a result of large imports from Sweden and the United Kingdom. A comparison of Canadian and United States trade in auto parts with other countries is shown in Exhibit 15, overleaf. No evidence was found to indicate that the very high degree of foreign ownership of the Canadian auto parts industry has distorted Canadian auto parts export trade with countries other than the United States.

The two important new factors could effect the potential behaviour of foreign-controlled firms with regard to export markets:

- the apparent concern in the United States to improve the current balance of payments position (by economic and political pressures to increase exports from the United States)

EXHIBIT 15

COMPARISON OF CANADIAN AND U.S. TRADE
IN AUTOPARTS WITH OTHER COUNTRIES, 1971
(Millions of U.S. Dollars)

	UNITED STATES	CANADA
Exports	Parts and Accessories	Parts and Accessories
Belgium & Luxembourg	27.1	-
France	18.0	1
West Germany	33.9	2
Italy	9.1	1
Netherlands	9.0	-
Sweden	15.0	5
United Kingdom	41.0	3
Japan	16.1	-
Mexico	143.0	22
Venezuela	50.2	5
South Africa	26.7	2
Philippines	21.5	1
Australia	55.6	23
Other Countries	255.8	13
Total:	722.0	78
Imports		
Belgium & Luxembourg	2.4	-
France	7.7	4
West Germany	157.4	4
Italy	6.0	1
Netherlands	1.5	-
Sweden	4.8	14
United Kingdom	62.9	29
Japan	156.3	15
Other Countries	32.0	20
Total:	431.0	87

SOURCE: Statistics Canada
Bureau of the Census (U.S.)

- the specific arrangements which have been introduced for special export corporations - Domestic International Sales Corporation (DISC) - as provided by the U.S. Revenue Act of 1971.

The DISC program in particular represents a serious threat to the freedom of United States subsidiary companies in Canada to export to markets outside of North America. The effects of the DISC program are not yet evident. It seems likely to affect adversely the performance of the Canadian auto parts industry in markets outside of North America if the program achieves a measure of success.

IV - ATTITUDES REGARDING POSSIBLE GOVERNMENT POLICY INITIATIVES

In the course of interviews with executives in the industry, a number of possible areas for government policy initiatives were discussed. There was uniformity of view towards government intervention in general - a strong "hands-off" approach - particularly regarding control over acquisitions or mergers. The acceptability to executives of more active government intervention decreased with seniority. Generally the industry is not sympathetic towards policies which involve direct intervention in corporate ownership. Some of the industry's concerns, however, are on matters related to ownership and control, e.g. the industry's concern for improved export performance.

ATTITUDE TO NATIONALISM

The executives interviewed were not nationalistic. They regard the auto parts industry as a North American industry. Their customers are United States companies. For some firms a major proportion of their sales are to plants of those firms on United States soil, and made under duty free arrangements.

Some Canadian executives in Canadian-controlled companies were outspoken in their contempt for the "issue" of foreign ownership as a whole. Others felt that perhaps increased or unrestricted foreign ownership would make it difficult for Canadians to separate themselves from the United States in the future, but they considered that the economic benefits of foreign investment outweighed these

"vague possibilities". Executives in the industry consider that the economic benefits of United States investment justify the presumed dangers of over-reliance on that country, and the corresponding loss of Canadian identity. Most executives feel that it is possible (at present) to reap the benefits of foreign capital investment in Canada, and "still maintain a distinctly Canadian way of life". Executives were vague as to the length of time over which this distinct way of life could be maintained. Their views were oriented almost totally to the present, with little if any concern for the long-run effect.

To observers familiar with the political, economic, and social aspects of foreign ownership, and well versed in the viewpoints of those who comment on and discuss the foreign ownership issue, the views of many of the auto parts industry executives appear to be based on only fleeting or casual attention to written or spoken comment on the issue, and little or no independent thought. It is not suggested that in this respect they are any different from any similar group of executives in any other industry.

In an industry in which foreign ownership controls between 85 per cent and 95 per cent of activity, executives who have achieved senior management positions in the industry and who, to a large extent (i.e. 85 per cent to 95 per cent) are employed by foreign-controlled firms, perhaps not unnaturally regard such circumstances as a fact of business life. They have long since become used to these circumstances, and accept them. They themselves have achieved personal success in spite of foreign ownership and have seen their firms expand.

However, the economic dangers which follow from a lack of control over Canadian economic activity that is associated with a "branch plant" economy are recognized by executives in the auto parts industry, and this appreciation has increased in the last one to two years with the realization of the growth of American economic nationalism, and the introduction of such measures as the DISC program. In general the industry's suggestion is not to prevent or reverse the present control pattern by government legislation, but to increase the long-term competitive strength of Canadian-controlled companies by encouraging investment by Canadians in Canadian-controlled activities, and by the selective (but non-discriminatory) use of government financial aid.

GOVERNMENT CONTROL OF MERGERS AND ACQUISITIONS

The firms examined had only limited exposure to merger and acquisition activity. Firm C1, a Canadian-controlled firm, had acquired a number of manufacturing companies, not all in auto parts manufacture. Firm A1, the largest firm, and foreign-controlled, had made one acquisition, and local management anticipated more acquisition activity.

Executives in one Canadian-controlled firm considered their firm at a disadvantage because of its small size relative to competition - which in this case was mainly from larger companies in the United States. There was some support for government assistance in the formation of larger firms by merger, in order to achieve production levels which would support better research and development, and carry the costs associated with more effective selling efforts.

Firm C1, with experience of merger and acquisition activity supported the need for larger firms, and the suggestion that governments might encourage and assist this process. However, the president of Firm C1 was skeptical that government support could improve the success rate of mergers which, in his experience, was determined by the personalities of key executives in the merging firms.

There appears to be no clear answer to the question of whether larger firms are needed in the industry. The automotive industry fluctuates according to the general level of economic activity, and the larger firms are equally susceptible to the effects of such fluctuations. The creation of firms which are diversified (into non-automotive business) may provide some protection against the full impact of sudden reductions in auto parts sales, but the Canadian-controlled firm with diverse interests created by merger (Firm C1) was the firm with the least attractive financial performance in the last five years. The very successful Firm B, was not large but was able to establish itself in a specialized market for a technical product, against competition from larger firms. However, this Firm had received considerable technical assistance and "know-how" from its United States partner at the time of the Auto Pact.

Each firm's circumstances with regard to economies of scale varies according to the type of product manufactured and the extent to which the product and/or the manufacturing process lends itself to research and development effort, the hiring of specialist skills, or an upgrading of sales and marketing expertise. Where the product is

designed and specified in detail by the automotive manufacturer, economies of scale will depend largely on the nature of the manufacturing process. In the case of high value products requiring greater technology, and where competitive strength demands greater research and development, and skilled sales effort at the automotive manufactures plant, the financial, technical, and managerial resources which may be more readily available from a larger group are most likely to pay off.

Executives interviewed gave no support to measures to exert government control of take-over of Canadian firms. There would be no support for the prohibition of the sale of a company to foreign interests. The main reason for this view was the belief that Canadian entrepreneurs - or shareholders - should be free to sell their interests to the highest bidder.

ISSUE OF CORPORATE STOCK ON CANADIAN EXCHANGE

Government policies designed to encourage or require foreign-controlled companies to issue stock to Canadian investors through Canadian stock exchanges would be favoured by a number of Canadian executives. Such policies would be seen as a way of replacing foreign risk capital with Canadian risk capital and so, in the long term, lead to the creation of the capital resources necessary to reduce the extent of foreign ownership. Canadian nationals working for foreign-controlled firms showed particular interest in these possible policies, but their interest was largely financial i.e. to obtain a "stake" in the company

for which they worked and share its profits, rather than a conscious interest in establishing more Canadian ownership. In the larger foreign-controlled companies the Canadian operation appears to be an attractive investment to senior management of those companies. This would seem to indicate that such companies are viable as distinct Canadian entities.

GOVERNMENT PROGRAMS
OF FINANCIAL AID

Existing government programs designed to provide financial support for research and development - P.A.I.T. and I.R.D.I.A. - were commended by executives in the industry and there was evidence of the value of these programs to the firms interviewed. Some executives considered that the programs could be made more effective by relaxing some of the conditions contained in the program regulations, particularly regarding accounting details, and the assessment of overhead costs attributable to R & D programs.

Some of the firms examined also spoke favourably of the Automotive Adjustment Assistance Program and two of the firms examined were among those firms which took immediate advantage of the loans available from the A.A.A. at the time it was initiated in 1965. The use of the A.A.A. by firms in the industry suggests the value of its being reinstituted. The Automotive Adjustment Assistance Program officially terminated its role as a lending authority as of June 30, 1973. At that time there was an outstanding loan balance of $75 million and this will be paid off as per agreed terms. Manufacturers requiring investment loans can qualify under what is known as the expanded Gatt Program. Under this program

prospective borrowers make their own loan arrangements with an appropriate financial institution, and the Federal Department of Industry Trade and Commerce insure the loan.

With any kind of financial assistance through government programs, all executives would object to schemes which discriminated against foreign-controlled firms by providing assistance to Canadian-controlled firms only.

THE ENCOURAGEMENT OF INVESTMENT IN CANADIAN FIRMS

Executives interviewed in the seven auto parts firms were unanimous in the view that Canadians are reluctant to invest in business enterprise, compared with, say, citizens of the United States. This reluctance is considered to be the reason for the difficulty of raising risk or venture capital for business opportunities in Canada, and many firms have experienced a similar conservatism among the chartered banks.

Executives feel that in the long run, only the internal development of investment capital can reduce foreign ownership of capital in the Canadian economy as a whole. Policies which are considered to support this objective of capital formation include lower personal taxation, a degree of tax relief on investment income from Canadian-controlled corporations (or discrimination against foreign investment income), and a rebate on capital gains obtained on Canadian investments.

EXPORT INCENTIVES

A number of executives interviewed expressed particular concern at the potential impact of the U.S. DISC program. As a result of this program there will be an incentive to U.S. firms to

supply the Canadian market from U.S. based plants. Thus the domestic market for auto parts will become more competitive for Canadian firms, and the possible growth of U.S. economic nationalism will tend to curb the efforts of Canadian-controlled firms to expand exports to the United States. Both of these effects may encourage Canadian firms to seek other markets outside of North America, but the terms of the DISC program will tend to give U.S. firms the same advantages in these markets also.

A number of executives commented very strongly that Canada needs to find an answer to the DISC program, and the lack of any Canadian response to the program (initiated in mid-1971) is criticized. None of the executives who expressed this view had suggestions to make regarding the possible response to DISC, and, as mentioned earlier in this report, the effects of the program on the auto parts industry in Canada are not yet evident.

V - CONCLUSIONS AND POLICY CONSIDERATIONS

CONCLUSIONS

Limitations of This Survey

The auto parts industry in Canada is made up of a large number of firms which represent wide variations in size, management sophistication, and competitive strength. It is a multiproduct industry and business conditions, and opportunities are not the same for all firms and for all products.

The seven firms examined in this study were chosen because of variations in size, products, control, and other factors. The auto parts industry is heterogeneous and the small number of firms examined emphasizes the need to be cautious in drawing conclusions for the whole industry.

Importance of the Industry

For Canada, and particularly for Ontario, the auto parts industry is a vital and large part of secondary manufacturing activity. The industry is a major employer, and a user and developer of important manufacturing processes and technologies. It is in Canadian interests to maintain the competitiveness and prosperity of the auto parts industry. The level of employment in the industry, the importance of the industry to Canada's balance of payments with the United States, and the multiplier effect of its activity all point to the need to maintain the industry in a viable and healthy state.

Behavioural Differences
Between Foreign-Controlled
and Canadian-Controlled Firms

The automotive parts industry in Canada is an integral part of an industry which is North American in terms of markets, ownership and control, and business attitudes. It is a highly competitive industry and in general, the behaviour of firms in the industry and the attitudes of executives do not differ according to whether the firm is foreign- or Canadian-controlled.

The behaviour of autoparts firms with regard to financing, community involvement, and exports to countries outside of North America does not differ significantly as a result of control characteristics. The extent and nature of the control of firms does influence the degree of local management autonomy of a Canadian subsidiary. However, the extent of local autonomy enjoyed by foreign-controlled subsidaries varies widely, and the management of many foreign-controlled firms will enjoy greater autonomy than the management of many Canadian-controlled firms. Management of the Canadian-controlled subsidiary can expect the same type of business decisions and the same degree of control by the parent corporation as the firm which is foreign-controlled. There is no evidence, for example, that a Canadian parent corporation would be more lenient with regard to lay-offs during slow-downs in the industry than would its foreign counterpart.

Local autonomy of firms in the auto parts industry can be expected to be subservient to corporate priorities and business opportunities particularly as parent companies diversify into different industries and develop subsidiary activities in a wider range of countries. In practice, the behavior of the firms examined suggests that the growth and prosperity of the auto parts industry in Canada over the last eight years has provided attractive investment opportunities in Canada for foreign-controlled and Canadian-controlled firms alike, and local management has had little if any difficulty in obtaining approval for expansion plans. There is no guarantee that this will continue to be the case in the future. Firms controlled by parent corporations in the United States may be influenced by political pressures on the parent corporations.

There is evidence that foreign-controlled firms have benefited from their connections with a large parent corporation in <u>obtaining an entry into</u> the <u>Detroit</u> based purchasing divisions of the major automative manufacturing firms. Although most firms, foreign-controlled and Canadian-controlled, have established sales offices in Detroit the Canadian-controlled firms may have been at some disadvantage compared to their foreign-controlled competitors. This disadvantage was felt most strongly in the years immediately following the signing of the Canada-U.S. Auto Pact in 1965. The future effect of this advantage enjoyed by foreign-controlled firms is difficult to estimate. It must be assumed that the influence of a large auto parts parent corporation in the United

States of the automotive manufacturers will continue to provide some advantage to foreign-controlled firms compared with Canadian-controlled firms, particularly the smaller firms.

Many firms in the auto parts industry do little if any research and development. Often such effort is of limited value because the automotive manufacturer defines the product to be manufactured and the auto parts manufacturer acts as a "jobbing shop". Research and development is more important in the case of complex products requiring high technology. Some Canadian and foreign-controlled firms are operating in this high-technology area. Most foreign-controlled firms have access to central corporate research and development activities centered outside of Canada. Because of the large size of the parent corporation these facilities can be expected to exceed similar facilities available to Canadian-controlled firms.

It is difficult to measure or quantify the extent to which the Canadian-controlled firm is at a disadvantage with respect to research and development compared to the foreign-controlled firm. No examples were identified of business being lost by a Canadian-controlled firm to a foreign-controlled firm because of product or process advantages which resulted from the foreign-controlled firm's access to extensive reseach and development facilities. This possible disadvantage is alleviated to some extent by the availability of government programs such as PAIT and IRDIA, and these programs are used by many firms, regardless of their

control. Although precise figures are not available, an examination of the products of the firms in this industry suggests that the high value technology based products are generally manufactured by firms which are foreign-controlled. To a large extent this would appear to be due to the historical development of the industry in the United States, and the expansion of specialist firms manufacturing products such as wheels, frames, brakes, etc. through the development of subsidiary companies in Canada and other countries. Without major research and development effort, Canadian-controlled firms are unlikely able to enter or maintain themselves, in this "high technology" section of the auto parts market.

The Effect of Foreign Control

In the auto parts industry the extent of foreign control, measured by dollar investment, is in the range 85 percent to 95 per cent. This high percentage of foreign control is not a recent development, and extends back to the period prior to the 1965 Auto Pact. There is limited data to indicate whether this percentage is increasing or decreasing. We conclude on the basis of our examination that there has been no significant increase in the percentage of foreign control in recent years, but executives of foreign-controlled firms showed interest in making acquisitions, although not necessarily confining this activity to the auto parts industry. There is evidence that Canadian-controlled companies are equally acquisition-minded (see Exhibit 11, page 24).

In the past, and particularly since the Auto Pact in 1965, the extent of foreign control in this industry appears to have had a significant impact on productivity and competition. This is because foreign-

controlled firms have been able to import from their parent corporation, skilled personnel, manufacturing technology, and investment capital. This infusion, combined with the Auto Pact, has created a highly competitive climate in the industry and Canadian-controlled firms have largely responded favourably to these influences, and in order to survive, have frequently matched their foreign-controlled counterparts in terms of productivity, cost controls, and quality. Having regard for the performance of the industry, particularly in the period 1961 to 1969 when the motor vehicles and parts industry achieved an increase in productivity of 199 per cent, and taking into account the growth of exports of parts to the United States and its beneficial effect on Canada's balance of trade with that country, it must be concluded that some aspects of foreign control have been instrumental in creating considerable economic benefits for Ontario and Canada as a whole. However, Canadian-controlled firms now appear capable of developing their own technology improvements on a par with their foreign-controlled competitors. Future benefits which may be obtained by the infusion of technology through foreign-control are likely to be less important to the economy than they were immediately following the signing of the Auto Pact.

Set against these advantages of foreign control in the industry is the extent and nature of decisions made by parent corporations outside of Canada which may operate against Canadian interests. Such decisions may relate to:

- lay-offs and employment practices
- the transfer of earnings from Canada to the parent Corporation
- the sourcing of production for exports

- requirements to purchase machinery, equipment and supplies from outside Canada
- the employment of foreign nationals
- location of R & D activities outside of Canada

Except for the question of employment to foreign nationals the study produced no evidence to support the view that discrimination against Canadian interests in these ways is commonplace. There was no evidence that foreign-controlled firms received direction from corporate level with regard to lay-offs, although they do receive assistance and direction in associated areas, particularly with regard to union negotiations. The most subordinated foreign-controlled firm had the best record with regard to lay-offs.

Similarly, there was no evidence that foreign-controlled firms were forced to repatriate earnings at the expense of further expansion and investment in Canadian operations. Although earnings may often exceed the funds required for capital investment and the surplus be repatriated, there was no suggestion that such repatriation (presumably for investment outside of Canada) occured when competitive investment opportunities existed in Canada.

The evidence regarding the sourcing of production for export is less certain. The level of exports from the typical auto parts firm is so low in relation to total output, and so little attention is paid to export opportunities by most firms, that the channeling of export opportunities to foreign based plants rather than Canadian based plants may occur but be unknown to local Canadian management. However, an

examination of the relationship between exports and total production of the auto parts industry in the United States, with the same relationship in Canada indicates no significant difference in export performance by the two countries.

The proportion of machinery and equipment expenditures spent in Canada as against the import of equipment varies considerably from firm to firm. Data obtained in the study suggests that foreign-controlled corporations may be more likely to purchase machinery and equipment from outside of Canada, possibly in conjunction with the parent corporation, but the information available is so limited as to make this a very tentative conclusion. It was clear from discussions with one foreign-controlled firm that the firm had made every effort to purchase equipment in Canada in spite of the fact that for certain specialized equipment Canadian manufacturing capability was highly suspect.

It is clear from the study that the employment of foreign nationals in senior positions is more likely to be found among foreign-controlled firms, and these appointments will frequently be made at the instigation of the parent company. The positive aspects of such behavior - the value of importing special skills not available in Canada - has been eliminated by the development of the industry in Canada in the last eight years, and the availability, in general, of Canadians or Canadian residents with comparable skills. However, there is no evidence to support a policy of erecting barriers to the transfer of U.S. nationals into Canada, so long as Canadians have a comparable ease of access to positions in the U.S.A..

Expenditures on research and development varied widely among the companies studied and appeared to depend on a variety of factors, including corporate size and product line, rather than country of ownership. While it could not be determined conclusively, Canadian-controlled companies in some product lines appeared to conduct as much research and development as their foreign-controlled counterparts in comparable business situations. Nevertheless, in the overall North American context, partly as a result of the "Big Four" auto assemblers', leadership indications are that proportionately more research and development is being conducted in the U.S. than in Canada.

POLICY CONSIDERATIONS

Future Developments

A real concern must exist regarding the possible impact of foreign control if other influences are brought to bear on parent corporations outside of Canada, leading them to make decisions regarding Canadian subsidiaries other than those that they would make under normal business conditions. Such influences include political pressure to increase employment in certain areas of the United States, financial inducements to set up manufacturing activities in other countries rather than in Canada, and political pressures to restrict the imports into the United States of auto parts from Canada for balance of payments considerations. There is a strong feeling in the auto parts industry in Canada that such influences have increased in the last one to two years.

Assuming that Canadian auto parts firms can remain competitive with United States based auto parts firms, in terms of productivity, price, and quality, and by the necessary degrees of research and development, then foreign control over much of the auto parts industry is unlikely to markedly interfere with the Canadian trade balance in this industry so long as North American trade in auto parts is relatively free and unrestricted.

The only firm example of such influences (discussed on page 43) which was obtained in the course of the study was a case of discrimination against Canadian production by a United States based automotive manufacturer, rather than by the parent corporation of the auto parts firm operating in Canada. All of the industry's customers for original equipment are foreign-controlled and could, from time to time, take a similar position. There was a strong feeling among executives in the industry that Unites States sentiments with regard to the Auto Pact had changed significantly from a readiness to buy Canadian parts to a coolness towards importing Canadian products. The companies examined, however, were unable to quantify the affects of this change in attitude.

To some extent the change in attitude reflects the success of both foreign-controlled and Canadian-controlled auto parts companies in Canada in the years since the Auto Pact. The 1965 Auto Pact was not unanimously approved by interested groups in the United States, and improvement in balance of trade for Canada in automotive parts has led to strong representations for action to improve this balance in favour of the United States. It is difficult to attribute this situation to the

extent of foreign control in the Canadian industry. If the auto parts industry in Canada were 100 per cent Canadian-controlled, and equally successful in exporting products into the United States than the resulting favorable balance of trade in auto products must be assumed to be at least as much a concern to the United States as it is under actual present conditions. It also seems likely that, in this industry, political pressure on the foreign-controlled automobile manufacturers would be as effective in deterring Canadian made auto parts imports as would pressure on the more numerous parent offices of foreign-controlled subsidiaries in Canada.

Where government pressure on foreign parents is most important in the future is on the development of exports. Under the influence of the DISC program or in response to other pressures it would be relatively easy for aaparent corporation to regard its Canadian subsidiary as a captive supplier to the Canadian automobile market, and concentrate on developing export business from its United States based plants. Such developments could hold back the development of exports to countries outside of North America by firms operating in Canada. In any future Auto Pact renegotiations some guarantees against this possibility could be an objective of Canadian negotiation, subject to further studies in the nature of export potential in this industry.

Reduction in the Extent of Foreign Control

The Canadian auto parts industry is predominantly foreign controlled, and the industry would object to measures which attempted to achieve a reversal of this situation by compulsory means. Compulsion to

sell to Canada or to Canadians would thus alienate the industry, and increase the uncertainty with regard to future foreign investment in Canada. The acquisition of foreign-controlled firms at market value by government agencies e.g. the Canada Development Corporation, would be acceptable in principle, providing it could be supported in terms of the availability of Canadian capital which would be necessary, and in terms of the management direction which would also be required.

The large amounts of both public and private capital required to increase the extent of Canadian ownership of the auto parts industry may be more beneficially deployed in obtaining control of other industries, or of making investments in new industries. This study has revealed no basis for making the Canadianization of the auto parts industry a high priority. The two main alternatives are to acquire control of what already exists, or to establish policies which will assist Canadians to acquire and maintain control of future growth areas of the industry. It is therefore important to devise policies which lead to an adequate level of capital formation, and the investment of capital in Canadian-controlled enterprises with significant growth potential in the auto parts industry. The industry is still a long-term growth industry, and one in which new products and new technology should be anticipated. The development of the rotary engine, computerized ignition and other systems, and the possible future development of electrical powered cars and revolutionary new public transit systems suggests that the dynamics of the industry will provide new areas for growth, and hence new areas for Canadian investment.

Canadian investment. Complete foreign ownership of the "Big Four" auto manufacturers, however, means that in the absence of major Canadian government programs, the initiative for such development will tend to come from the United States; thus resulting "demand pull" for technological innovation by auto parts manufacturers will therefore continue to be felt more strongly in the United States than in Canada.

The existing capability of Canadian-controlled auto parts firms to capitalize independently on such developments is limited, since the necessary research and development may well be beyond the resources of the programs of most, if not all, of these firms. Government financial support of research and development programs will therefore be necessary to ensure a satisfactory share of future growth for Canadian-controlled firms. To be fully effective such programs would need to provide assistance in the application of new technology, including assistance in marketing and production.

On the basis of this scenario, two policies could be considered: (1) Government policies to ensure the continuation of the restricted free trade in auto parts; and (2) government policies to ensure that Canadian-controlled firms can obtain the necessary support in their attempt to remain competitive, particularly in relation to the need for research and development in high technology product areas. The present disadvantage suffered by Canadian-controlled companies with respect to research and development will adversely affect the competitive strength of these companies in the long term. Without adequate research and

development activity Canadian-controlled companies in the industry may be forced away from the manufacture of the more complex and technical products into the less complex and lower value products where research and development is less important.

The industry is heavily reliant on the United States for its market, but for a number of years the United States has pressed for renegotiation of the Auto Pact. The Canadian industry therefore needs to establish new growth areas in markets outside of North America. The initiative for diversification of the industry's markets may be dependent on government encouragement, unless restriction of the U.S. market forces auto parts firms in Canada to look for markets outside of North America.

Possible Government Policy Initiatives

It is in Canadian interests to maintain the competitiveness and prosperity of the auto parts industry, regardless of ownership. In order to achieve this objective government policies both at provincial and federal levels should be designed to assist the industry in those areas most critical to its continued success. The Canadian Government should be alert to changes in attitude on the part of the United States, and develop well researched and properly conceived policies to counter United States attitudes to the Auto Pact, legislation such as the DISC program which may be harmful to the auto parts industry, and the less definite, but still potentially unfavorable trend toward protectionist policy in the United States. Canadian policy should be designed to

maintain the free trade aspects of the 1965 Auto Pact but with a more flexible approach to the safeguards regarding Canadian value added.

Present policies at federal and provincial levels with regard to export activities should be reviewed in the light of the particular problems of exporting auto parts outside of North America. The objectives of such a policy should be to reduce the dependence of the Canadian auto parts industry on the United States, while at the same time improving the balance of trade in auto parts with countries outside of North America.

Existing government policies which support research and development should be reviewed in order to identify ways in which greater support can be given to firms carrying out research in high technology areas.

Increased Canadian control of the industry should be based on ownership acquired under normal market conditions. Such control will be dependent on the investment of risk capital. Policies should be devised which, in the long run, can influence the degree of control of the auto parts industry exerted by Canadians by the development of a larger capital base in Canada and the investment by public agencies or by private individuals in Canadian-controlled firms which have considerable potential in areas of new technology and new products.

APPENDIX A

ONTARIO SELECT COMMITTEE ON ECONOMIC AND CULTURAL NATIONALISM

MANAGEMENT OPINION QUESTIONNAIRE FOR THE AUTO PARTS INDUSTRY STUDY

These questions were used as a basis for interviews conducted by the KPM consultant with senior management personnel in each company.

These questions were not designed for self-completion.

1. MARKETS, COMPETITION, EXPORTS

1.1 How has your market changed in the last five years (more exports, less automotive etc.)? What are the growth areas? The decline areas?

1.2 How has competition changed in the last five years? What are your competitive advantages/disadvantages vis-a-vis other firms (particularly those whose ownership is foreign/Canadian in contrast to yours).

1.3 Are Canadian owned A.P. manufacturers too small to compete successfully with foreign owned firms?

1.4 Do Canadian A.P. manufacturers need continued government protection in order to survive competition from foreign controlled firms?

1.5 Do subsidiaries of foreign controlled firms have exporting disadvantages if the parent firm is also exporting (either directly or through international divisions)?

1.6 What is needed (government aid, rationalization, etc.) to increase Canadian A.P. exports?

1.7 What is the greatest barrier to exports of your company?

1.8 Do you use government agencies for export promotion and advice?

2. LOCAL AUTONOMY AND AUTHORITY

2.1 Do you think local management of foreign controlled firms have little autonomy on decisions related to investment, labour management, local community affairs?

2.2 What limits apply to your purchasing decisions ($ levels or sources)? What is the procedure with larger purchases?

2.3 What are your levels of authority regarding:

(a) senior management

(b) plant labour.

2.4 What is your role in long-range planning?

2.5 What is your authority on:

- market strategy
- advertising decisions
- choice of advertising agency
- choice of engineering consultants.
- product development
- expansion investment
- productivity improvement

3. INDUSTRY RATIONALIZATION

3.1 The Gray Report published by the Government of Canada in 1972 recommended a federal screening authority to examine and rule on some or all of the following types of foreign investment situations:

(a) takeovers of Canadian firms by foreign interests

(b) new direct investment by foreigners in Canada

(c) licensing, franchising and long-term supply contracts with foreigners

(d) expansion of existing foreign controlled firms in Canada

(e) behaviour of Canadian-controlled multinational firms.

Federal legislation is now being prepared regarding the first three items listed above. Do you agree or disagree that some sort of government review or control procedure is required?

3.2 Should steps be taken to provide relatively more working capital to Canadian business men, such as government supported loans, allowing banks to take equity positions in Canadian enterprises, restricting the proportion of funds which Canadian banks can lend to foreign interests operating in Canada?

3.3 To what extent do you think the Canadian A.P. industry should rely on government help in the form of an auto pact or tariff policy?

3.4 Has the Auto Pact saved Canadian A.P. firms from gradual decline?

3.5 Should the government introduce measures to prevent any more Canadian A.P. firms being taken over by foreign controlled firms?

3.6 Do you have any plans to diversify out of automotive parts manufacture?

3.7 What was the effect of the Auto Pact on your company:

- sales
- employment
- profit
- competitiveness, etc.

4. <u>COMMUNITY INVOLVEMENT</u>

4.1 How does your firm support local community activities? What is your policy?

4.2 Do you think that Canadian controlled firms behave differently from those that are foreign controlled with respect to support of the local community?

5. <u>EMPLOYMENT</u>

5.1 Do you see differences in working conditions, pay, or salaries between foreign controlled and Canadian controlled firms?

5.2 Are senior management positions in foreign controlled firms frequently filled by foreign nationals?

5.3 Do ambitious Canadian managers in foreign controlled A.P. firms have to look to parent organizations outside of Canada in order to maximize their career potential?

5.4 Do foreign and Canadian controlled firms behave differently with regard to:

- plant stoppages
- unemployment issues
- recruitment.

6. RESEARCH AND DEVELOPMENT

6.1 Do you actively engage in R & D? What kind of R & D?

6.2 How much do you rely on your parent for corporate R & D?

6.3 Is R & D too costly for Canadian A.P. firms?

7. FINANCIAL

7.1 Do U.S. auto manufacturers prefer to obtain parts from Canadian suppliers with U.S. parents who also supply?

7.2 Do the corporate resources of U.S. controlled A.P. firms in Canada enable these firms to achieve higher manufacturing efficiency than comparable Canadian firms?

7.3 Should Canadian owned A.P. manufacturers receive more help from the government in the form of investment grants for new machinery and equipment?

7.4 It has been argued that corporate tax reductions should be granted to firms in proportion to their earnings from exports of manufactured goods, with these reductions applying less strongly to firms with greater degrees of foreign ownership.

Do you agree or disagree with some or all of this suggestion?

8. ADVERTISING AND ENGINEERING

8.1 (a) What was the total amount you spent on engineering consultants last year?

(b) To what extent did you use engineering service provided by your own staff? Staff of the parent company?

9. <u>NATIONALISTIC ATTITUDES</u>

9.1 The Gray Report says that foreign ownership in Canada probably leads to the distortion of industrial priorities, export restrictions, import propensities, lowering of research and product development and, in general, truncation of full economic and entrepreneurial activities by firms in this country.

Do you agree or not with this general conclusion or parts of it?

9.2 Some people think that the pervasiveness of foreign-controlled companies in Canada is producing a "made in U.S.A." culture in Canada, in terms of television programs, advertising, publishing, educational material, the types of goods and services which are available, and the way in which social priorities are set and achieved.

Do you agree or disagree with this general statement?

9.3 Some people feel that all large companies operating in Canada (say net worth of $250 million or more or annual profits of $10 million or more) should be required to become 51% or more owned by Canadian citizens, with this to take place, in accordance with suggested government legislation, over the next five to ten years. Coupled with this should be the provision, effective more immediately, that all senior executives and a majority of the Board of Directors of such firms must be Canadian citizens.

Do you agree or disagree that this would be an appropriate government action to maintain Canadian economic and cultural sovereignty?

9.4 Some people feel we should require foreign-owned firms in Canada to list their shares on Canadian exchanges and make available a large minority holding to Canadian investors in this way. It has also been suggested that shares of firms operating in Canada should <u>not</u> be listed on U.S. stock exchanges, in order to encourage relatively more investment in these companies by Canadians.

Do you agree with either of these suggestions?

9.5 Should the government require, or provide incentives to encourage, purchase of Canadian materials, components and services, not only by government departments but also by large companies operating in Canada, in an effort to create and expand Canadian employment in high technology and related areas?

Do you agree or disagree that the Canadian labour movement should conduct its affairs more independently than at present with regard to "parent" unions in the U.S.?

CONFIDENTIAL

FOREIGN OWNERSHIP STUDY

STATISTICAL QUESTIONNAIRE

This questionnaire consists of statistical or factual questions which are designed to assist the Select Committee's consultants (Kates, Peat, Marwick & Co.) to properly interpret the opinions of senior management regarding foreign ownership issues.

THE INFORMATION REQUESTED WILL BE CONFIDENTIAL. IT WILL BE ARRANGED WITH THAT OF OTHER FIRMS AND THE FACT THAT YOUR FIRM WAS A SOURCE OF INFORMATION WILL NOT BE DISCLOSED TO THE COMMITTEE WITHOUT YOUR PRIOR APPROVAL

Your co-operation in this study is appreciated.

CONFIDENTIAL QUESTIONNAIRE

AUTOMOTIVE PARTS INDUSTRY

1. Please complete for your business for the last full year for which information is available:

   Year: 197

   Total Sales, all products $ __________

   Total Sales, automotive parts $ __________

PERCENTAGE OF TOTAL SALES $

	Sales to Customers in: Canada	U.S.	Other Export	Total Sales
Automotive				
OEM				
Aftermarket				
Total				
Other Markets				
Total				

2. Please provide the same information as in question #1 for the previous 4 years.

3. Please give details of your total employment:

TOTAL PERSONS EMPLOYED

	Canada (excl. Ontario)		Ontario		Total	
	Automotive Parts	Other	Automotive Parts	Other	Automotive Parts	Other
1968						
1969						
1970						
1971						
1972						

4. Please list, with numbers employed, those manufacturing locations in Ontario which you have expanded or reduced in the last 5 years:

	YEAR	LOCATION	EMPLOYMENT CREATED/(REDUCED)
Expanded Plants			
Reduced Plants			

* Note: please indicate new plants (N) and plants which have been closed (C)

5. Please show as a percentage of total sales revenue from automotive parts the amount of your expenditures on research and development in Canada. Only research and development expenditure (including engineering, design, development and testing) should be shown:

	Sales Revenue From Automotive Parts $	Expenditure on Research and Development $	Percentage of R & D Expenditures Carried Out by Canadian Staff or Contractors
1972			
1971			
1970			
1969			
1968			

6. Please indicate your main competition by market by inserting as appropriate the words, "stronger", "strong", "not competitive", or "no effective competition", in the following table.

	Canadian Controlled Firms in Canada	Foreign Controlled Firms in Canada *		Foreign Controlled Firms Outside *		Captive Plants
		U.S. Owned	Other	U.S.	Other	
After Market						
O.E.M.						

* Excluding captive plants i.e. plants or companies which are subsidaries of your customers.

7. Of your total expenditures on new marketing and production equipment in each of the last 5 years please show the percentage which was of Canadian origin.

MACHINERY AND PRODUCTION EQUIPMENT

YEAR	TOTAL CAPITAL EXPENDITURE	CAPITAL EXPENDITURE ON EQUIPMENT OF CANADIAN ORIGIN	%
1972			
1971			
1970			
1969			
1968			

8. Please indicate the extent to which your business (either OEM or AM) is dependent on a small number of customers by completing the following table as appropriate.

ORIGINAL EQUIPMENT MARKET

OEM PRODUCT LINE	PERCENTAGE OF SALES TO 1 CUSTOMER				
	Up to 10%	11% to 20%	21% to 40%	41% to 60%	Over 60%

AFTER MARKET

AM PRODUCT LINE	PERCENTAGE OF SALES TO 1 CUSTOMER				
	Up to 10%	11% to 20%	21% to 40%	41% to 60%	Over 60%

9. Approximately what percentage of your stock is owned outside of Canada?

10. Of 1972 capital requirements what percentage was obtained from:

Stock sold in Canada	________
Canadian banks	________
U.S. or other foreign banks	________
Retained earnings	________
Other (please specify)	________
	100%